



1 APPEARANCES: (Cont'd)

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6  
7 (Appearing on behalf of the Citizens  
8 Utilities Company of Illinois and  
9 Citizens Lake Water Company)

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17 (Appearing on behalf of the Illinois  
18 Industrial Water Consumers)

19

20

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(Appearing on behalf of the Staff of the  
Illinois Commerce Commission)

21 SULLIVAN REPORTING COMPANY, by  
22 Cheryl A. Davis, Reporter, CSR #084-001662  
Carla J. Boehl, Reporter, CSR #084-002710

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3	JOSEPH F. HARTNETT, JR.				
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8	RONALD D. STAFFORD				
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1	I N D E X		
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3	IAWC 1.0, 1.1, 1.2, 1.0R, 1.0SR, 1.3SR		487
4	IAWC 2.0, 2.1, 2.2, 2.0R, 2.1R, 2.2R, 2.3R, 2.0SR, 2.4SR		611
6	IAWC 3.0, 3.1 - 3.5, 3.0R, 3.1R, 3.5R, 3.6R, 3.0SR		530
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1 PROCEEDINGS

2 EXAMINER SHOWTIS: Pursuant to the authority  
3 vested in me by the Commerce Commission, I now call  
4 for hearing Docket 00-0476 which concerns the  
5 petition of Illinois-American Water Company,  
6 Citizens Utilities Company of Illinois, and  
7 Citizens Lake Water Company for approval of a  
8 proposed reorganization and affiliated interest  
9 agreements, issuance of common stock and debt  
10 securities and assumption of affiliated interest.

11 Will the parties please enter their  
12 appearances for the record.

13 MR. SPRINGER: Boyd J. Springer and Lidia  
14 Fiore of Jones, Day, Reavis & Pogue, 77 West  
15 Wacker, Suite 3500, Chicago, Illinois 60601-1692,  
16 appearing on behalf of Illinois-American Water  
17 Company.

18 MS. SCHULTZ: Sue Schultz, General Counsel of  
19 Illinois-American Water Company, also appearing on  
20 behalf Illinois-American. My business address is  
21 300 North Water Works Drive, Belleville, Illinois  
22 62223, and my telephone number is (618)239-2225.

1           MS. CONTI: Lee Ann Conti, 1000 International  
2           Parkway, Woodridge, Illinois 60157, appearing on  
3           behalf of Citizens Utilities Company of Illinois  
4           and Citizens Lake Water Company.

5           MS. VON QUALEN: Janis Von Qualen and Joseph  
6           T. Clennon, on behalf of the Staff of the Illinois  
7           Commerce Commission, 527 East Capitol Avenue,  
8           Springfield, Illinois 62701.

9           MR. FITZHENRY: Edward Fitzhenry with the law  
10          firm of Lueders, Robertson and Konzen, Post Office  
11          Box 735, Granite City, Illinois 62040, appearing on  
12          behalf of the Illinois Industrial Water Consumers.

13          EXAMINER SHOWTIS: I believe Mr. Hartnett will  
14          be the first witness today.

15          MR. SPRINGER: Yes, Mr. Examiner. We're ready  
16          to proceed.

17          EXAMINER SHOWTIS: You may proceed.

18          MR. SPRINGER: Thank you.

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22

1 JOSEPH F. HARTNETT, JR.  
2 called as a witness on behalf of the Joint  
3 Applicants, having been first duly sworn, was  
4 examined and testified as follows:

5 DIRECT EXAMINATION

6 BY MR. SPRINGER:

7 Q. Please state your name and business  
8 address.

9 THE WITNESS:

10 A. My name is Joseph F. Hartnett, Jr. My  
11 address is 1025 Laurel Oak Road, Voorhees, New  
12 Jersey 08043.

13 Q. And, Mr. Hartnett, by whom are you  
14 employed?

15 A. I'm employed by American Water Works  
16 Service Company as the Vice President of Finance.  
17 I also serve as the Treasurer of American Water  
18 Works Company.

19 Q. And have you prepared testimony for  
20 purposes of this case?

21 A. Yes, I have.

22 Q. I show you what's marked as IAWC Exhibit

1 4.0 and ask if that is a copy of direct testimony  
2 that you've prepared for this proceeding?

3 A. That's correct.

4 Q. I also show you a copy of what's been  
5 marked for identification as IAWC Exhibit 4.0R and  
6 ask if that is a copy of rebuttal testimony --

7 A. That's correct.

8 Q. -- that you prepared for this case?

9 A. That is correct.

10 Q. And in that testimony do you sponsor  
11 what's been marked as IAWC Exhibit 4.1R?

12 A. That is correct.

13 Q. Do you also sponsor surrebuttal  
14 testimony which has been marked as IAWC Exhibit  
15 4.0SR?

16 A. Yes, that's correct.

17 Q. Is the information presented in the  
18 testimony and the exhibits you sponsor true and  
19 correct to the best of your knowledge?

20 A. Yes, it is.

21 MR. SPRINGER: At this time, Mr. Examiner, I  
22 would ask for admission into evidence of

1 Mr. Hartnett's direct testimony, Exhibit 4.0, his  
2 rebuttal testimony, Exhibit 4.0R, surrebuttal  
3 testimony, Exhibit 4.0SR, and Exhibit 4.1R which  
4 Mr. Hartnett sponsors in his rebuttal testimony.

5 EXAMINER SHOWTIS: Is there any objection?

6 MR. CLENNON: Staff has one objection -- or  
7 two objections, Your Honor.

8 EXAMINER SHOWTIS: Okay.

9 MR. CLENNON: In Mr. Hartnett's rebuttal  
10 testimony on page 2, line 6, as well as page 4,  
11 line 11, Mr. Hartnett first of all says Mr. Smith  
12 does not appear to understand our proposal. This  
13 is complete speculation, beyond this witness's  
14 ability to know. The same thing with page 4;  
15 Ms. Langfeldt clearly does not understand the SSP.  
16 Once again, this is beyond the witness's knowledge.  
17 The comments create a setting of animus in this  
18 proceeding that is completely uncalled for, and  
19 they should not be permitted to be entered into the  
20 record.

21 EXAMINER SHOWTIS: A response?

22 MR. SPRINGER: May I respond, Mr. Examiner?

1 EXAMINER SHOWTIS: Yes.

2 MR. SPRINGER: Mr. Examiner, the comments  
3 referred to are not intended to create any feeling  
4 of animus or comment on anything in an  
5 inappropriate way. The comments are directed to  
6 testimony of the witnesses and are indicating that  
7 the witness does not understand the proposal in the  
8 context of the testimony given, and I don't think  
9 there's anything inappropriate in commenting in  
10 that manner.

11 MR. CLENNON: Your Honor, it's clearly beyond  
12 his ability to understand. In addition to this,  
13 we've, you know, gone through a day of testimony  
14 where -- verbal testimony where these matters are  
15 becoming more and more apparent. The Company  
16 should be able to put on its case without resorting  
17 to these tactics.

18 MR. SPRINGER: Again, I don't think there's  
19 anything inappropriate in commenting that testimony  
20 reflects a misunderstanding of a proposal.

21 EXAMINER SHOWTIS: The motion to strike those  
22 portions of the testimony is denied, and I would

1 state for the record I do know what animus means.

2 (Laughter)

3 Is there any other motions?

4 MR. CLENNON: No other objection, Your Honor.

5 EXAMINER SHOWTIS: Okay. Mr. Hartnett is  
6 available for cross.

7 MR. SPRINGER: Is there a ruling on the  
8 exhibits?

9 EXAMINER SHOWTIS: I think I -- well, you're  
10 right. The exhibits sponsored by Mr. Hartnett are  
11 admitted.

12 (Whereupon IAWC Exhibits  
13 4.0, 4.0R, 4.1R, and 4.0SR  
14 were received into  
15 evidence.)

16 MR. SPRINGER: Thank you.

17 Mr. Hartnett is available for  
18 cross-examination.

19 MR. FITZHENRY: I don't have any questions.

20 MR. CLENNON: Okay.

21 MR. FITZHENRY: Maybe I'll have some after  
22 you're done.

1           MR. CLENNON: Staff has some questions. May I  
2 proceed, Your Honor?

3           EXAMINER SHOWTIS: Yes, you may.

4                           CROSS EXAMINATION

5           BY MR. CLENNON:

6           Q.     Good morning Mr. Hartnett. As you know,  
7 my name is Joe Clennon.

8           A.     Good morning.

9           Q.     I represent the Staff of the Illinois  
10 Commerce Commission.

11                    Could you please turn to your  
12 surrebuttal testimony, sir? And lines 78 to 80.

13          A.     Yes, I have that.

14          Q.     Okay. There you state, as stated in my  
15 response to Data Request RL 8.02, the DCF analysis  
16 was updated to reflect tax benefits during our  
17 negotiations with Citizens. Is that a fair  
18 reading, sir?

19          A.     Yes, that's correct.

20          Q.     Sir, can you explain to me and to this  
21 court why this updated DCF analysis was not  
22 provided in response to Staff Data Request 1.02?

1           A.     I don't recall Staff Data Request 1.02.

2           Q.     It's the Hart-Scott-Rodino filing.

3           A.     It was not included in the Hart-Scott-  
4     Rodino filing.

5           Q.     Can you explain to me why this  
6     information was not provided in response to Staff  
7     Data Request 1.05?

8           MR. SPRINGER: Can you state the number again,  
9     Mr. Clennon?

10          MR. CLENNON: 1.05, Staff Data Request 1.05.

11          MR. SPRINGER: All right. That's not TQS?

12          MR. CLENNON: No, it is not.

13          MR. SPRINGER: Okay. Just a moment.

14                   (Pause in the proceedings.)

15          A.     The Staff Data Request 1.05 I don't  
16     believe -- we put this together -- we put this  
17     summary together for submission with the data  
18     response specifically. We didn't -- I don't  
19     believe back in July we would have had this put  
20     together when the data response was requested or  
21     data request was asked. As we were going through  
22     the negotiations with Citizens, as we gained

1 additional information we would keep track and  
2 maybe update our numbers on a piece of paper, but  
3 we didn't necessarily rerun a full DCF and a full  
4 formal presentation as we gave -- as we presented  
5 as a response to the data request. We pulled that  
6 together specifically in response to the data  
7 request.

8 Q. Your testimony, sir, states that the DCF  
9 analysis was updated to reflect the tax benefits  
10 during our negotiations with Citizens. Is that  
11 correct?

12 A. That's correct.

13 Q. And the data request is dated July 24,  
14 2000. Is that correct?

15 A. Right.

16 Q. And that is after the negotiations with  
17 Citizens.

18 A. That's correct.

19 Q. Is that correct?

20 A. That's correct.

21 Q. Can you explain to me why, when the DCF  
22 analysis was updated during the negotiations with

1 Citizens, it was not provided on July 24th?

2 A. The DCF analysis that was provided in  
3 response to 1.02 was the initial DCF analysis. We  
4 quantified the tax benefits afterwards, did a  
5 separate DCF, and came up with a separate number  
6 and just added that to I think it was 722 million  
7 in the initial DCF, so we didn't run a new,  
8 combined DCF.

9 Q. And when you updated that, that was  
10 during the negotiations. Is that correct?

11 A. That's correct.

12 Q. And then that was not provided to the  
13 Staff after the Staff asked for it in Data Request  
14 5.01. I'm sorry; 1.05.

15 A. The copy that we provided was the only  
16 copy of the analysis available. We would have done  
17 a calculation of the present value of the tax  
18 benefits, but we wouldn't have done a -- we didn't  
19 have a copy of any analysis.

20 Q. Do you have a copy of RL -- Data Request  
21 RL 2.15?

22 A. Yes, I have it.

1           Q.     In part, that data request asks were the  
2     valuation methods identified and demonstrated by  
3     Mr. Bobba identical to the valuation techniques  
4     employed by IAWC in determining the purchase price  
5     for the utility assets, and your answer, in part,  
6     says in addition to those factors, the parent  
7     employed a discounted cash flow analysis. This  
8     analysis is included in Attachment 4(c)-6 to Data  
9     Request 1.02, and this was issued -- this data  
10    request was received by you on September 7, 2000.

11   Why was not this information provided in September?

12           A.     Well, as I said previously, the  
13    calculations we did we started out with the first  
14    DCF which was \$722 million. As we got more  
15    information from Citizens or as we gained more  
16    information from our tax advisors, we might do a --  
17    we might say, okay, we have an additional 20  
18    million of value related to the tax benefits, so we  
19    might have done either on a side -- on a piece of  
20    paper or -- there was no formal rerun DCF done at  
21    that time. So as we were building the information  
22    and gaining information from Citizens during the

1 negotiation process, we were updating the value we  
2 had identified. We didn't pull together and  
3 resubmit anything to the board or do a whole new  
4 DCF because it was still within the authorization  
5 or the range that we had to negotiate with  
6 Citizens, so we didn't have to do a formal  
7 presentation to do that so we didn't do it until  
8 such time as --

9 Q. And you did not provide it with --

10 MR. SPRINGER: I don't think the witness has  
11 completed his statements.

12 EXAMINER SHOWTIS: Finish your answer.

13 A. I'm finished.

14 Q. Isn't it true, sir, that for Staff Data  
15 Request DAB 1.5, as well as DAB 1.6, again, you did  
16 not provide this analysis that you had done during  
17 the negotiations with Citizens?

18 MR. SPRINGER: I object to the word analysis.  
19 I believe the witness specified that he did not  
20 consider what was done to be an analysis.

21 MR. CLENNON: Your Honor, his testimony  
22 clearly states that the DCF analysis was updated to

1 reflect tax benefits during our negotiations with  
2 Citizens. The Staff asked for this information,  
3 and this witness in particular states that it was  
4 updated and then it is not provided by the company.  
5 I would like to have an explanation on why Data  
6 Request DAB 1.5 and DAB 1.6 was not updated with  
7 this information when it was specifically asked  
8 for.

9 MR. SPRINGER: Is that the question now?

10 MR. CLENNON: Yes. That was the question  
11 originally.

12 EXAMINER SHOWTIS: You can answer that  
13 question.

14 A. The DCF analysis was not updated. We  
15 ran separate calculations as we gained additional  
16 information and just added the result of those  
17 calculations to the original DCF. We did not do a  
18 new DCF analysis to reflect all of these new -- all  
19 these pieces of new information until requested to  
20 combine them all together -- until requested as  
21 part of the 8.04 or 8.02 request by Ms. Langfeldt.

22 Q. If you take a look at Data Request DAB

1 1.6, that data request says, if yes, please provide  
2 all documents presenting and supporting the  
3 analysis that Mr. Hartnett reviewed. Once again,  
4 sir, you did not provide that. Is that correct?

5 A. I did not have any formal documents. If  
6 I did -- I do not recall having any documents that  
7 would have had the new \$895 million number that was  
8 provided. That was done -- if we did it, we did it  
9 on a separate piece of paper, a scratch paper,  
10 which I did not save.

11 Q. Sir, does it not say please provide all  
12 documents?

13 A. Yes.

14 Q. Does not say formal documents?

15 A. I don't think I have any documents,  
16 formal or informal.

17 Q. If we could turn to page 2 of your  
18 direct. I'm sorry; page 3, please, line 11. You  
19 indicate at that point in your testimony that you  
20 were involved in the acquisition of the water and  
21 wastewater assets of Citizens, including contact  
22 with Citizens executives. Is that correct?

1           A.     I'm sorry. I don't have the right  
2 reference I don't think. Line 11 of page 3?

3           EXAMINER SHOWTIS: I think you have the wrong  
4 cite.

5           Q.     I'm sorry. I'm looking for page 2. I  
6 apologize.

7           A.     No problem. Line 11, page 2. Yes, I  
8 have that.

9           Q.     In there you say that you were involved  
10 in all aspects of the investigation to purchase the  
11 assets from Citizens. Is that true?

12          A.     That's correct.

13          Q.     And that included the assembly and  
14 analysis for public information concerning  
15 Citizens, including reports to the state public  
16 utility commissions, the SEC filings, contracts,  
17 investigations, development of financial analysis.  
18 Is that true?

19          A.     The conduct of due diligence  
20 investigation. Yes, that's correct.

21          Q.     And you were involved in all of those  
22 aspects?

1           A.     Yes, I was.

2           Q.     Would it be also true that in connection  
3     with your position as Vice President of American  
4     Water Works, you were contacted -- you were in  
5     contact with other American Water Works executives  
6     concerning the purchase?

7           A.     I was in contact with members of the due  
8     diligence team, some of which are executives in  
9     other subsidiaries, yes.

10          Q.     And is it your testimony now that you  
11     had no contact with other executives while you were  
12     assembling the analysis of all the information  
13     concerning Citizens' water and wastewater  
14     properties? Is that your testimony now?

15          A.     I was in contact with executives at  
16     American Water Works Company at the corporate  
17     headquarters.

18          Q.     Okay.

19          A.     And the members of the due diligence  
20     team, but I wasn't necessarily in contact with all  
21     the executives at the subsidiary level.

22          Q.     Okay. Were you in contact with all the

1 executives at American Water Works Company?

2 A. Yes, many of the executives, yes.

3 Q. Many of the executives?

4 A. Yes.

5 Q. During your performance of these duties  
6 that you have listed here?

7 A. Yes, I was.

8 Q. I would assume that it is also correct  
9 that you were in contact with the Board of  
10 Directors of American Water Works from time to  
11 time. Is that true?

12 A. At least we did submit the presentation  
13 to the Board of Directors one time.

14 Q. During your performance of your duties  
15 concerning the purchase of Citizens, did you ever  
16 contact customers of either Citizens or  
17 Illinois-American Water Company?

18 A. No, I did not.

19 Q. On page 2 of your testimony you speak of  
20 a public teleconference call between Citizens and  
21 certain financial analysts. Did you participate in  
22 that call?

1           A.     I did not participate. I listened to  
2     it, yes.

3           Q.     Okay. So would it be true that your  
4     testimony on page 2, the sentence that begins on  
5     line 24, in early June, we participated in a public  
6     teleconference call between Citizens and certain  
7     financial analysts during Citizens' discussion of  
8     recent acquisition of telecommunication properties  
9     from GTE and further discussed their intention to  
10    sell wastewater and water products should be  
11    changed to in early June we listened?

12          A.     I guess technically that's correct. I  
13    apologize.

14          Q.     Can you identify for this court and for  
15    me the parties that were participating or listening  
16    in on that phone call?

17          A.     No. I do not know that.

18          Q.     Do you know if there were any customers  
19    of Citizens that participated in that phone call?

20          A.     I do not know that.

21          Q.     On page 3 of your testimony you talk  
22    about a mid June meeting involving American Water

1 Works and Citizens executives. Did this meeting  
2 relate to the purchase of the Citizens properties?

3 A. Yes. It related, as I say in the  
4 testimony, we were expressing our interest in  
5 acquiring the water and wastewater properties.

6 Q. Were any customers participants of this  
7 meeting?

8 A. No.

9 Q. Were any customer groups such as CUB  
10 participants of this meeting?

11 A. I'm sorry. I don't know what CUB is.

12 Q. Oh, I'm sorry; the Citizens Utility  
13 Board here in Illinois.

14 A. Citizens Utility? There were no  
15 customers participating in the meeting.

16 Q. All right. There were any customer  
17 advocate groups participating?

18 A. No, not to my -- no, there were not.

19 Q. Is it correct, sir that, no customers or  
20 customer advocacy groups of either Citizens or  
21 Illinois-American negotiated any aspect of the  
22 purchase?

1           A.     Certainly not as a large group.  Whether  
2     some of the Citizens executives might have been  
3     customers of their water utilities I don't know,  
4     but, no, not a big group.

5           Q.     A very good distinction.  Thank you.

6                     As an executive for American Water  
7     Works, would you recommend that the stockholders of  
8     that company or a utility either directly or  
9     through an agent in negotiations for the purchase  
10    of an asset prior to the stockholders assuming the  
11    risk of that purchase -- I'm sorry.  Let me start  
12    that over.  Let me just skip that one.

13                    Would you turn to page 3, beginning on  
14    line 4?

15          A.     Yes.

16          Q.     There you state that Illinois-American  
17    or American Water Works accumulated information on  
18    Citizens to determine the preliminary value of  
19    Citizens' water and wastewater properties.  Is that  
20    a correct -- a fair reading of your testimony?

21          A.     Yes, that's substantially correct, yes.

22          Q.     Was one of your concerns surrounding the

1 valuation of these assets for the purpose -- was  
2 one of your concerns surrounding the valuation of  
3 the assets the potential risk to shareholders?

4 A. At that time, certainly you're  
5 considering that, but this is a nonbinding  
6 expression of interest so you're not as focused on  
7 the risks at that point. You're trying to  
8 determine what the fair value of the assets is.  
9 Subsequently, certainly we consider the risk to the  
10 shareholders, certainly.

11 Q. I believe on page 3, line 10, you  
12 discuss Citizens' relationship with Morgan Stanley  
13 Dean Witter as its advisor.

14 A. That's correct.

15 Q. Is it your understanding that Morgan  
16 Stanley provided advice to the Board of Directors  
17 of Citizens?

18 A. I don't know whether -- I can't say  
19 whether they provided advice to the Board of  
20 Directors. I know they were advising management.  
21 I would imagine they probably provided advice, but  
22 I don't know that for a fact.

1           Q.     I believe on page 3 you speak of a  
2     confidentiality agreement with Citizens.

3           A.     Yes.

4           Q.     And that was needed to conduct your due  
5     diligence. Is that correct?

6           A.     That's correct.

7           Q.     And this obligation of due diligence,  
8     that's an obligation to the board of directors, is  
9     it not?

10          A.     Among others. It's a process certainly  
11     to go through to determine the level of interest  
12     you have in an acquisition, and you're certainly  
13     considering -- it's an obligation to the board of  
14     directors, the shareholders, and all constituents.

15          Q.     And just so I'm clear, the  
16     confidentiality agreement was needed so you could  
17     fulfill the due diligence obligation. Is that  
18     correct?

19          A.     That's correct.

20          Q.     Do you believe that the existence of the  
21     confidentiality agreement inhibited participation  
22     by customers or customers advocacy groups in the

1 negotiations?

2 A. I'm not quite sure what you mean.

3 Certainly the confidentiality agreement did limit  
4 how many people you could talk to, since Citizens  
5 Utilities was a publicly traded company and there's  
6 restrictions on disclosure of non-public  
7 information, restrictions in the securities laws.  
8 I don't think the confidentiality agreement in and  
9 of itself would have prohibited -- well, I don't  
10 think the confidentiality agreement was the reason  
11 that the customers were not present at the  
12 negotiations.

13 Q. Very good. But certainly it limited the  
14 Company's ability to contact customer groups.

15 A. It did, but more as a result of the  
16 securities laws, potential securities laws  
17 violations of disclosing non-public information.

18 Q. Very good.

19 On page 3 you discuss intensive  
20 negotiations that were conducted by AWS [sic] and  
21 Citizens from September 10th till July 24th, after  
22 which point Citizens released an offering document

1 to other potential bidders for water and wastewater  
2 assets; I'm sorry, for wastewater -- for the water  
3 and wastewater assets.

4 EXAMINER SHOWTIS: I think you misspoke. It  
5 was from September 10th to September 24th. You  
6 said July 24th.

7 MR. CLENNON: I'm sorry. I'll still stuck on  
8 that data request.

9 MR. SPRINGER: Did you also reference AWW or  
10 was that AWW?

11 MR. CLENNON: AWW.

12 A. AWW, in my testimony, did conduct --  
13 that's correct, did conduct significant  
14 discussions, extensive discussions between  
15 September 10th and September 24th. That's correct.

16 Q. Moving on, if a bid is made and a  
17 purchase occurs, just generally, does the bid --  
18 does the bidder, by virtue of the purchase, assume  
19 the risk of ownership?

20 A. The bid itself doesn't assume the risk  
21 of ownership. If you close, there are certain  
22 risks in the transaction.

1           Q.     Very good.

2                     Is it reasonable that if a potential  
3 bidder chooses not to make a bid and make the  
4 purchase, one of the factors could be that that  
5 bidder was not interested in assuming the ownership  
6 risk of that investment?

7           A.     There are many, many different reasons  
8 that a bidder might not choose. That could be one  
9 of the reasons. I agree that could be one.

10          Q.     But generally, investors are risk  
11 adverse.

12          A.     No, I wouldn't say risk adverse. I  
13 would say they expect a return commensurate with  
14 the risk they take.

15          Q.     So part of their analysis is the risk  
16 involved with a certain investment. Is that  
17 correct?

18          A.     That's correct.

19          Q.     To your knowledge, did any customers of  
20 Citizens make a bid on the purchase of the company?

21          A.     I have no knowledge of any other  
22 bidders, the other bidders for Citizens.

1           Q.     If you could turn to page 4, beginning  
2     on lines 19, I think of your surrebuttal testimony  
3     actually.

4           A.     That's surrebuttal, page 4?

5           Q.     Yes.

6           A.     And what line number is that?

7           Q.     Line 19.

8           A.     I have a different sequence.

9           MS. SCHULTZ:  There's no 19 on 4.

10          Q.     Okay.  I apologize.

11          A.     79 is --

12          Q.     Hold on.  Let me just slow everybody  
13     down.  I'll find the right one.

14                     (Pause in the proceedings.)

15           I'm sorry.  It was in your direct  
16     testimony.  I apologize for the inconvenience.

17          A.     No problem.  What page was that?

18          Q.     Page 4.

19          A.     Yes, I have it.

20          Q.     You state something along the lines of  
21     in today's economy, the values of companies in  
22     nearly every industry are above book value.  Is

1     that a fair reading?

2             A.     That's correct.

3             Q.     Isn't it true, sir, that nearly every  
4     industry does not share the monopolistic  
5     environment that the water industry shares?

6             A.     That's correct.

7             Q.     Could you get out Data Request RL 2.03,  
8     please?

9             A.     Yes, I have it.

10            Q.     In there I believe you indicate that you  
11     use -- that you considered the use of property  
12     plant and equipment net of depreciation as a basis  
13     for allocation of the project purchase price, but  
14     rejected this as an allocation method. Is that  
15     correct?

16            A.     Yes. We did think about that.

17            Q.     Isn't it true, sir, that the use of the  
18     allocation methodology that employs plant property  
19     and equipment net of depreciation distinguishes --  
20     has the ability to distinguish among state  
21     jurisdictions a proportion of the utility assets  
22     that the customers have already paid for through

1 rates?

2 A. I'm sorry. I don't really underst and  
3 the question.

4 Q. Okay. Property plant and equipment net  
5 of depreciation is an allocation methodology. Is  
6 that not correct, sir?

7 A. That is an allocation methodology.

8 Q. Good. And as an allocation methodology,  
9 it has the ability to distinguish among the state  
10 jurisdictions the proportion of utility assets that  
11 the ratepayers have already paid for. Isn't that  
12 correct?

13 A. While I'm not -- certainly not an expert  
14 in ratemaking, I don't believe the customers pay  
15 for depreciated plant. I believe -- I understand  
16 that in ratemaking, depreciated plant is a  
17 component of rate base upon which revenues are set.  
18 I do understand that.

19 Q. Okay. Would you agree, sir, that the  
20 use of this methodology helps enable the company or  
21 others to determine the proportion of utility  
22 assets by state jurisdictions that have been

1 recovered, the value of those assets that have been  
2 recovered by the company through its rates?

3 A. I can't say that I understand that.

4 MR. CLENNON: Staff has nothing further.

5 EXAMINER SHOWTIS: I have a few questions.

6 EXAMINATION

7 BY EXAMINER SHOWTIS:

8 Q. Would you turn to page 3 of your direct  
9 testimony?

10 A. Yes, I have that.

11 Q. In the last paragraph on that page,  
12 which carries over to page 4, you discuss time  
13 periods under which intensive negotiations were  
14 conducted, and you indicate on September 24th  
15 Citizens released an offering document to other  
16 potential bidders for the water assets. Would you  
17 just indicate to me what you mean by an offering  
18 document?

19 A. Sure. I would be happy to. Typically  
20 when a seller wants to sell assets or a company,  
21 they will conduct an auction, and they'll put  
22 together an offering memorandum which gives you the

1     basic financial information on the company, some  
2     background on the company and its assets. They put  
3     all that together as kind of a selling document to  
4     offer to potential bidders.

5           Q.     Was such a document given to AWW by  
6     Citizens before September 24th?

7           A.     No, it was not. Because we initiated  
8     the discussions with Citizens beginning in the  
9     summer of '99, they had not yet -- it came before  
10    the actual formal process that they were getting  
11    ready to put together, so they didn't have the  
12    offering memorandum available when we started  
13    discussions.

14          Q.     Is the purpose of providing the offering  
15    document to solicit possible bids from potential  
16    buyers?

17          A.     That is the initial piece of information  
18    that you are given as the potential buyer to  
19    solicit bids, but generally you get more  
20    information after that.

21          Q.     Okay. I don't need to know the names or  
22    details, but do you know if Citizens received any

1 other offers for its public utility assets?

2 A. I understand from hearing testimony in  
3 other states from Citizens' witnesses that they did  
4 receive other bids. Yes, Your Honor.

5 Q. Those would pertain to its assets in  
6 Illinois?

7 A. Yes. It was for the -- I think -- well,  
8 I just know they received other bids for the entire  
9 water and wastewater assets, including Illinois,  
10 yes.

11 Q. Okay. So would you consider AWW to be  
12 competing with other bidders for the assets of  
13 Citizens?

14 A. By the end of the process, we were  
15 definitely involved with a competitive bid  
16 situation as a result of these other bids coming  
17 in, yes.

18 Q. I asked a question of Mr. Hamilton I  
19 think that was deferred to you. The question was,  
20 in agreeing to the purchase price for the Citizens  
21 assets, what assumptions, if any, were made with  
22 regard to the ratemaking treatment of the

1 acquisition adjustment and sharing of savings?

2 A. We didn't have a specific sharing  
3 savings methodology in mind when we negotiated the  
4 purchase price. The underlying assumption we did  
5 make in arriving at the purchase price was that the  
6 commissions would treat the company in such a way  
7 to allow the company to retain the savings that  
8 were produced to cover the premium on the  
9 acquisition. We didn't know specifically and we  
10 didn't consider specifically how each commission  
11 might choose to do that or what the ultimate  
12 methodology would be that we would propose to the  
13 commission. We simply assumed that if we could  
14 adopt the tariffs from the existing customers, we  
15 would be able to retain the savings we produced  
16 below that or the savings we produced to offset the  
17 purchase price -- the premium; excuse me.

18 Q. Okay. Testimony has been presented by  
19 Illinois-American in this docket that approvals  
20 have been obtained in certain jurisdictions with  
21 regard to the purchase of Citizens' water and  
22 wastewater assets. Is that correct?

1           A.     That's correct.

2           Q.     Just so I understand the sequence of  
3     proposals with regard to the SSP, when was the  
4     specific SSP that's presented in this docket  
5     developed?

6           A.     That was developed by Illinois -American  
7     as part of their application process. I can't give  
8     you the specifics because I wasn't directly  
9     involved with the development of the proposal.

10          Q.     Do you know if the SSP or something  
11     comparable to the SSP was presented in other  
12     jurisdictions with regard to treatment of the  
13     acquisition premiums and savings in those other  
14     jurisdictions? I'm just trying to get an  
15     understanding if there's a proposal here that's  
16     different in certain respects or similar to what  
17     was presented in other jurisdictions.

18          A.     Yes. Four of the states do not require  
19     any ratemaking treatment as part of the approval  
20     process, so there was no discussion of ratemaking  
21     treatment in Pennsylvania where we just received  
22     approval, Ohio, and Indiana. Those ratemaking

1 treatments will be handled in the first rate case  
2 after the acquisition.

3 Q. So those orders wouldn't address any  
4 allocation of savings?

5 A. No. We made no proposal to them.

6 Q. Okay.

7 A. Arizona, that order is pending from the  
8 commission. However, we've reached a stipulation  
9 with the staff that they have agreed to consider  
10 the acquisition adjustment in relation to the  
11 savings presented at the first rate case, so,  
12 again, after the fact, not as part of the approval  
13 of the acquisition.

14 California is the only state of the six  
15 states involved here that does require a  
16 determination of the ratemaking treatment as part  
17 of the approval process, and there is a proposal in  
18 front of that commission for sharing of the savings  
19 and recognition of the acquisition adjustment.

20 Q. Do you know any details of that  
21 proposal? I'm just trying to see if it's  
22 comparable to like here we have 10 percent of the

1 savings to ratepayers initially and, you know, then  
2 it goes on from there, and I'm just trying to  
3 understand how the proposal in California compares  
4 to what's presented here.

5 A. Yes, Mr. Examiner. I'm generally  
6 familiar with it.

7 Q. I don't need a lot of details, but could  
8 you give me some of the highlights?

9 A. I can give you some of the highlights of  
10 what I recall. There is no rate proceeding for the  
11 first five years. There's a stay-out provision for  
12 five years.

13 Q. So more or less a rate freeze for five  
14 years?

15 A. Right. My recollection is we will then  
16 put forth in that first rate case at the end of  
17 five years the demonstration of our savings, and I  
18 believe we retain all savings approved in that  
19 first rate case to support the acquisition  
20 adjustment or the premium, and this is where I get  
21 fuzzy, and then we start sharing after we recover  
22 our full acquisition adjustment, but I'm not sure,

1     you know, and this is where I'm not real clear, but  
2     there's no savings sharing in the beginning in  
3     California. It's a stay-out and then the company  
4     recovers the acquisition adjustment from the  
5     savings generated at the end of five years based on  
6     proof of a rate case.

7             Q.     Okay.

8             A.     But please don't hold me to the details.

9             Q.     That's fine. But in California, the  
10     California commission would make some determination  
11     as to whether that proposal is appropriate? Is  
12     that what you're saying?

13            A.     Yeah, as part of the approval process,  
14     that's correct.

15            Q.     At what stage of the process are the  
16     proceedings before the California commission?

17            A.     The hearings are being continued.  
18     They've been interrupted until I think it's the end  
19     of February or early March they'll resume. The  
20     hearings should be completed. There should only be  
21     a very limited amount of hearing time remaining,  
22     but the hearings are not yet completed.

1 Q. Okay.

2 A. And if I might add, Mr. Examiner, the  
3 proposal in California, as it was here in Illinois,  
4 we tried to structure it in such a way to address  
5 the utilities in those states, the state of where  
6 those utilities are as far as ratemaking and things  
7 like that, to the particulars of the state.

8 Q. Just to summarize then what you said  
9 with regard to California, there's a five-year rate  
10 freeze, and in the first rate case the Company will  
11 present a demonstration of its savings. The  
12 proposal is that the Company will retain all  
13 savings until it has recovered the acquisition  
14 premium, and then after that there's some sharing  
15 mechanism.

16 A. Yeah. I believe it's until -- the  
17 Company will retain all savings to cover the  
18 acquisition revenue requirement, similar to here.

19 Q. Okay.

20 A. And I used the word premium. I  
21 apologize.

22 Q. That's fine.

1           A.     And then there's a sharing after that at  
2     some point, and I don't recall when that is and how  
3     that works.

4           Q.     If you know, in California is there --  
5     do you know the amortization period for the  
6     acquisition adjustment?

7           A.     Yes.  It's 40 years there also.

8           Q.     Okay.

9           A.     And the staff has -- we've stipulated  
10    with the staff on the amortization period as well  
11    as the estimation of the savings that we anticipate  
12    we can produce.  The staff and the Company have  
13    agreed and as to the methodology, should the  
14    Commission approve the transaction, as to how the  
15    Company would calculate the savings going forward  
16    over the 40 years.

17          Q.     So similar to Illinois, in California  
18    the Company's proposal is to amortize the  
19    acquisition adjustment over 40 years and also  
20    include the unamortized balance of that adjustment  
21    in rate base?

22          A.     I don't believe in our proposal we're

1 proposing to include the unamortized balance. I  
2 think we're sharing the savings. I don't believe  
3 we're including it in rate base.

4 Q. Okay.

5 A. In California I do believe there will be  
6 a determination at the end of that first rate case  
7 and an inclusion in rate base of it, but I won't  
8 swear to that.

9 Q. Okay. That's fine.

10 In your rebuttal testimony you reference  
11 on page 8 the DCF that was performed for CUCI that  
12 produced a value of 221 million.

13 A. Yes. I have that.

14 Q. Did the DCF analysis determine a maximum  
15 offer price range? In other words, did it come up  
16 with a range of figures?

17 A. Yes, Mr. Examiner. On the Exhibit 4.1R,  
18 if you look at the bottom of that schedule, you see  
19 the column headed F - Total Equity Value.

20 Q. I see those.

21 A. The range, depending on the different  
22 assumptions you use, you see the discount rates on

1 the left?

2 Q. Right. I see now. So for the 221  
3 million and the value shown there, the range was  
4 from 211.3 to 231.3. Is that correct?

5 A. Yes, that's correct, given the 10.3  
6 times EBITDA multiple.

7 (Whereupon a recess was  
8 taken at this time.)

9 EXAMINER SHOWTIS: Let's go back on the  
10 record.

11 Q. I just had one last question. If you'll  
12 turn to your surrebuttal testimony, page 2.

13 A. Yes.

14 Q. The sentence that begins at the end of  
15 line 28 reads as follows: "If IAWC does not have a  
16 reasonable opportunity to recover its investment in  
17 the acquisition by retaining a portion of the  
18 demonstrated savings, then IAWC does not believe  
19 Section 7-204 would be satisfied." Would you tell  
20 me what you meant when you used the words  
21 "reasonable opportunity to recover its investment"?

22 A. By reasonable opportunity I meant an

1 opportunity consistent with our proposal of savings  
2 of sharing -- or sharing of savings; excuse me.

3 Q. And would you just briefly describe what  
4 you meant by consistent with your proposal? Did  
5 you mean unless the proposal was adopted in its  
6 entirety, that IAWC does not believe Section 7-204  
7 would be satisfied, or did you mean there could be  
8 some conclusion reached by the Commission that  
9 would modify the proposal in some manner that would  
10 still satisfy Section 7-204?

11 A. I would say that the economics or the  
12 underlying economics of our proposal we have tried  
13 to stretch as much as we could to retain or to not  
14 harm the financial results of our Illinois-American  
15 subsidiary. We certainly understand there might be  
16 some other conditions placed -- non-economic  
17 conditions placed on the Commission, whether it's  
18 reporting information, things like that. However,  
19 me personally, as a financial person looking at the  
20 transaction, feel that we have provided as much of  
21 the benefits to the customer as we can in our  
22 Savings Sharing Proposal. Certainly we recognize

1 the Commission may reject the transaction. I'm not  
2 debating that. I'm just saying our proposal is  
3 stretching as far as I feel is appropriate from a  
4 financial person's standpoint.

5 EXAMINER SHOWTIS: Okay. That's all I had.

6 MR. SPRINGER: We do have some brief redirect,  
7 Mr. Examiner.

8 EXAMINER SHOWTIS: Okay.

9 REDIRECT EXAMINATION

10 BY MR. SPRINGER:

11 Q. Mr. Hartnett, in response to  
12 cross-examination questions, I believe you  
13 indicated that one of the factors considered was a  
14 goal that the transaction should be accomplished  
15 maintaining the existing tariffs of the acquired  
16 entity. Do you recall giving that response?

17 A. Yes, I do.

18 Q. And would you have a further explanation  
19 you'd care to give of the answer you gave?

20 A. Yes. The clarification is we would  
21 adopt the existing tariffs at closing, but the  
22 further emphasis I'd like to place is that the goal

1 I think in our proposal was that the rates would  
2 never increase higher than the rates CUCI would  
3 experience on a stand-alone basis, and, further,  
4 the reason we feel that's appropriate is because we  
5 are providing all the other benefits of being part  
6 of the American Water system to the customers that  
7 is included in Mr. Kelleher's testimony.

8 Q. So if I understand your answer, your  
9 reference to existing tariffs was not necessarily  
10 the tariffs presently in effect, but to tariffs no  
11 higher than stand-alone tariffs for CUCI would be.

12 A. That's correct.

13 Q. You also in response to a question of  
14 Mr. Clennon indicated that you did not know whether  
15 the net PP&E ratio if used as an allocator would  
16 distinguish between the portions of assets  
17 recovered through rates. Do you recall an answer  
18 of that nature?

19 A. Yes.

20 Q. Can you say whether you have any  
21 awareness of what the effect of applying that net  
22 PP&E allocator would be in the context of this

1 case?

2 A. Well, if we use net PP&E to allocate the  
3 purchase price across states, Illinois would  
4 actually get a marginally higher allocation of the  
5 purchase price, if that was the question. I was  
6 confused by the question, so I wasn't sure whether  
7 that answered the question or not.

8 Q. Now in response to questions of the  
9 Hearing Examiner, I believe you indicated that  
10 applications have been submitted with regard to  
11 this overall transaction in states other than  
12 Illinois, and I believe those states included  
13 California, Arizona, Pennsylvania, Indiana, and  
14 Ohio. Would that be correct?

15 A. That's correct.

16 Q. And you described in response to the  
17 Examiner's questions your understanding of the  
18 present situation in California. Is that correct?

19 A. Yes.

20 Q. Would you have any clarification of that  
21 discussion that you'd like to provide?

22 A. Yes. The term that I used that in

1 California we agreed to a five-year stay-out, which  
2 was I think also referred to as a freeze, I was  
3 mistaken. During the five years we have agreed to  
4 hold out for filing any rate increase related  
5 specifically to general and administrative costs.

6 Q. And with respect to Arizona, you  
7 discussed I believe a stipulation in place in that  
8 state. Is that correct?

9 A. That's correct.

10 Q. And would you have any further  
11 explanation of the provisions of that stipulation?

12 A. In that case there was a stipulation  
13 with the staff that they have agreed that they  
14 would consider recognition of an acquisition  
15 adjustment in the next rate proceeding commensurate  
16 with the demonstrated savings that the Company can  
17 put forth, and, furthermore, the staff has actually  
18 recommended approval of the acquisition.

19 Q. And with respect to the remaining  
20 states, you indicated that no approval -- or excuse  
21 me -- that the approval process for the transaction  
22 did not include consideration of a -- at that time

1 of the economic package or savings sharing  
2 proposals. Is that right?

3 A. There's no requirement. That's correct.  
4 There's no requirement for a determination of  
5 ratemaking for the acquisition adjustment.

6 Q. Do you have a basis for any expectations  
7 as to regulatory treatments when those proposals  
8 are ultimately presented at the time of rate  
9 proceedings in those states?

10 MR. CLENNON: Your Honor, I object to this  
11 question. It calls for speculation, well beyond  
12 the witness's ability to give an informed answer to  
13 this Commission, to this court and this Commission.

14 MR. SPRINGER: May I respond, Mr. Examiner?

15 EXAMINER SHOWTIS: Yes.

16 MR. SPRINGER: I don't believe there's any  
17 basis for Mr. Clennon's objection. Mr. Hartnett is  
18 an officer of the Company who has been involved in  
19 transactions in these states in the past, and I  
20 believe his answer will come from his personal  
21 experience and awareness of regulatory situations  
22 in the states involved.

1           EXAMINER SHOWTIS: He can answer the question  
2 as long as he ties his answer to how they've  
3 treated acquisition adjustments or premiums in past  
4 cases. If he doesn't have any knowledge of that, I  
5 will not allow him to speculate.

6           MR. SPRINGER:

7           Q.     Would you answer on that basis, please?

8           A.     Yes. In Pennsylvania, the last large  
9 transaction that I was involved with in  
10 Pennsylvania was Pennsylvania Gas and Water where  
11 we also purchased the water assets, a similar  
12 transaction to this Citizens transaction, and the  
13 Commission there recognized the full acquisition  
14 adjustment in rate base.

15                     In Indiana I was involved with the  
16 Avatar acquisition in 1993, and they are also -- as  
17 a fair value state, they recognized the fair value  
18 of the transaction, which recognized the full  
19 purchase price as fair value.

20                     I have no experience in Ohio.

21           Q.     Based on your experience in the states  
22 that are involved here, do you have an expectation

1 or have you experienced a situation in any of those  
2 states where the -- other than Illinois, where the  
3 regulatory commission staff has opposed recovery in  
4 any form of the costs associated with acquisition?

5 A. The staffs have not in any of the states  
6 opposed the transaction. As I said, they have not  
7 made a decision on the acquisition adjustment  
8 specifically. The staffs have not opposed any of  
9 the transactions though.

10 MR. SPRINGER: Thank you. That's all the  
11 questions that we have for Mr. Hartnett.

12 EXAMINER SHOWTIS: I just had a couple  
13 questions.

14 EXAMINATION

15 BY EXAMINER SHOWTIS:

16 Q. With regard to Arizona, you indicated  
17 that Staff indicated it would consider recognition  
18 of the acquisition adjustment in the next rate  
19 proceeding commensurate with demonstrated savings.  
20 What did you mean by consider?

21 A. I don't recall the specific language,  
22 Mr. Examiner, but there's very clear language that

1     they say they recognize the treatment of the  
2     acquisition adjustment or recognition in rates of  
3     the acquisition adjustment in some form, and how --  
4     again, how each commission chooses to do that would  
5     be considered in relation to the savings. I can't  
6     tell you. I don't have the exact language. I know  
7     I could get it if you gave me a minute, but.

8           Q.     No, that's fine.

9                     And with regard to the Pennsylvania Gas  
10     and Water case that you described, you indicated  
11     that the full acquisition adjustment was recognized  
12     in rate base. What was the treatment in that case  
13     of acquisition savings, and was there any rate  
14     freeze involved in that proceeding?

15           A.     There was no hold-out in that or rate  
16     freeze filed in that case. The savings -- they  
17     recognized the full purchase price in rate base, so  
18     the savings all flowed through to the customer.

19           EXAMINER SHOWTIS: Okay. That's all I had.

20           MR. CLENNON: I have some additional cross,  
21     sir.

22           EXAMINER SHOWTIS: Go ahead.

1 MR. CLENNON: May I proceed?

2 EXAMINER SHOWTIS: Yes.

3 RECROSS EXAMINATION

4 BY MR. CLENNON:

5 Q. When you stated in response to  
6 Mr. Springer's question that the use of the net  
7 PP&E allocation methodology will result in a higher  
8 allocation of the purchase price to the Illinois  
9 jurisdiction, is one of the factors that would lead  
10 to that higher allocation the fact that included in  
11 that would be the contributed capital Citizens  
12 carries on its books currently?

13 A. Net PP&E, as classified on the balance  
14 sheet, would include all the assets of the utility.  
15 Contributed capital is on the other side of the  
16 balance sheet, but it includes all assets in that  
17 PP&E.

18 Q. Very good.

19 You stated that I believe it's -- was it  
20 Avatar in Indiana?

21 A. Yes.

22 Q. Recognized the full value of the

1 acquisition adjustment?

2 A. They recognized the purchase price as  
3 fair value, yes.

4 Q. Fair value, and that is a fair value  
5 state?

6 A. That is.

7 Q. Do you know whether this Commission uses  
8 fair value?

9 A. I've heard representatives from our  
10 Company say Illinois is a fair value state, but I  
11 don't know that for a fact.

12 Q. Okay.

13 I believe you stated that the  
14 application in California there was some  
15 stipulation. Is that true?

16 A. A stipulation with the staff. That's  
17 correct.

18 Q. Is it your understanding that the staff  
19 approves the transfer of the assets or the merger  
20 reorganization?

21 A. No, the staff does not approve our  
22 proposal as filed. The staff simply stipulated

1     that they agree with the quantification of the  
2     savings that we had on file there.

3           Q.     Just so I understand your testimony, in  
4     Ohio there has been a filing by the commission  
5     stating approval of the transaction?

6           A.     Yes, that's correct.

7           Q.     Indiana?

8           A.     They've approved it also.

9           Q.     Pennsylvania?

10          A.     They have approved it.

11          Q.     Arizona?

12          A.     Arizona is awaiting a decision.

13          Q.     Can you describe what has taken place in  
14     that case so far?

15          A.     Yes. We've conducted hearings, reached  
16     stipulation with the staff, including their  
17     recommended approval. I think somebody testified  
18     yesterday that before the administrative law judge  
19     could write their recommendation, they very  
20     fortunately took an extended leave, so we are  
21     awaiting a recommended decision.

22          Q.     That's in Arizona, the extended leave?

1           A.     Yes.

2           Q.     Not in California?

3           A.     Yes.

4           Q.     Just for my own understanding, when you

5           said testified, was there prefiled testimony

6           submitted? Is that how that works?

7           A.     In Arizona?

8           Q.     Arizona.

9           A.     I believe there was, yes, as part of the

10          application.

11          Q.     In all the states is it similar to here?

12          A.     I believe that's correct, but I don't

13          know that.

14          Q.     In California there was a stipulation?

15          A.     No, California the hearings are still in

16          process. There has been a stipulation with the

17          staff on the numbers projected over 40 years.

18          Q.     Do you have Staff Data Request 1.0?

19          A.     No, I don't have that.

20          Q.     I'm sorry; 1.02.

21          A.     Is that the big one?

22          Q.     The big one.

1 (Whereupon said document  
2 was provided to the witness  
3 by Ms. Fiore.)

4 A. Yes, I have it.

5 Q. The request asked the Company to provide  
6 copies of all petitions, requests, applications,  
7 notices, or any other type of filing, whether  
8 formal or informal, requesting the approval and/or  
9 giving notice by or to any federal, state, or local  
10 regulatory agency of the acquisition of the  
11 Citizens Company by American. Is that correct?

12 A. I don't have the specific data request,  
13 but subject to check.

14 Q. And can you tell me why the Staff was  
15 not provided with the testimony, stipulations,  
16 orders in these other proceedings?

17 A. I don't believe I responded to that data  
18 request, did I?

19 Q. I understand that. Can you tell us why  
20 the Staff was not provided with this information?

21 MR. SPRINGER: I'm going to object. The  
22 question assumes facts not in evidence.

1           MR. CLENNON: Your Honor, it's a simple  
2 question. If he has no knowledge of it, that's  
3 fine.

4           EXAMINER SHOWTIS: Well, you can ask him if he  
5 knows whether there was a response. If he doesn't,  
6 then I think that that would end it for this  
7 witness.

8           MR. CLENNON: Very good.

9           Q. Do you know whether this response was  
10 updated as this material became available?

11          A. No, I have no knowledge.

12          MR. CLENNON: Your Honor, at this time I would  
13 like to make a motion to strike this testimony  
14 about the other jurisdictions. We have asked the  
15 Company to provide this information to us so we  
16 could prepare for this hearing, and it has not  
17 come. This witness said there was a stipulation  
18 when, in fact, on cross-examination we find out  
19 that there is no stipulation; in fact, that the  
20 staff of the other commission opposes the  
21 transaction. This is evidence that Staff should  
22 have the ability as well as the Intervenors to

1       respond to, and it is unacceptable.

2               MR. SPRINGER:   Mr. Examiner, may I respond?

3               EXAMINER SHOWTIS:   Yes.

4               MR. SPRINGER:   Mr. Hartnett has been  
5       responding to questions on cross-examination,  
6       redirect, and recross examination.   I don't know  
7       that there were objections to any of these  
8       questions as we went along, but that would be the  
9       timely approach.

10               I'm, quite frankly, not sure what has  
11       not been provided.   There's been a reference to a  
12       data request which was responded to.   I didn't  
13       recall any wording there about updates or requested  
14       updates, but I'm not sure there would have been any  
15       obligation to provide updates even had that been  
16       stated.   I believe all data requests have been  
17       fully responded to.   I'm not aware of any  
18       objections that have been submitted or any --  
19       really any problem with discovery in this case on  
20       either -- on the part of any party, so I believe  
21       this objection is inappropriate.

22               MR. CLENNON:   Your Honor, they have an

1 absolute obligation to update the data requests as  
2 time goes by, and this Company in this particular  
3 case has not been doing so.

4 As far as the timeliness of the  
5 objection --

6 EXAMINER SHOWTIS: I'm prepared -- I think  
7 I've heard enough about this.

8 I was the one who inquired about what's  
9 going on in other states, and I wanted to get some  
10 background as to how the proposal here fits with  
11 the proposals in other states and what the other  
12 commissions have done, so I'm going to deny the  
13 motion to strike. If you want to indicate in your  
14 brief the Company relies at all on what happens in  
15 other states, that no weight should be given to  
16 that, you're free to do so, but I think it's better  
17 for the record to have some information on what's  
18 going on in the other states with regard to this  
19 transaction. By striking it, there would be  
20 nothing in the record with regard to that.

21 MR. FITZHENRY: May I --

22 EXAMINER SHOWTIS: This information may -- I'm

1 not saying that this information necessarily is  
2 correct in all respects, but this is what this  
3 witness has given with regard to his understanding.

4 MR. FITZHENRY: Notwithstanding the Staff  
5 motion, the fact is that you have asked questions  
6 of this witness pertaining to these other  
7 jurisdictions, and certainly the record is not  
8 complete today as to, you know, what is in these  
9 orders and what is in these stipulations. The fact  
10 is we don't even know really the docket numbers or  
11 the style of these proceedings that Mr. Hartnet t  
12 has alluded to at great length, so what I would  
13 suggest, again, notwithstanding Staff's motion,  
14 that there be an on-the-record data request  
15 requiring the Company to produce to the Staff and  
16 Intervenors the stipulations that were entered into  
17 between the Company in California and Arizona,  
18 copies of any final orders that have been entered  
19 in the other states where other comparable  
20 transactions are being considered by jurisdictions  
21 I believe in Indiana and Ohio and Pennsylvania. We  
22 ought to have a chance to look at those orders and

1 comment on them in briefs, as you suggest, and we  
2 can't do that unless we're provided the orders,  
3 provided the dockets and the styles and the case  
4 numbers and so forth.

5 EXAMINER SHOWTIS: I think that's a reasonable  
6 request. I think if there are stipulations, there  
7 are orders, they should be provided to both Staff  
8 and IIWC if they want to address that in their  
9 briefs, so I think that's the best way of dealing  
10 with this. Make sure that information gets to  
11 Staff and IIWC, and if they want to review that and  
12 comment that some information provided by this  
13 witness is inconsistent with that, they can do so  
14 in their briefs.

15 MR. CLENNON: Your Honor, just so the record  
16 is clear, the instructions for the data request  
17 asked for updates, so the fact that it is not  
18 listed in the data request, it is listed in the  
19 instructions.

20 EXAMINER SHOWTIS: Okay. That's fine.

21 MR. SPRINGER: Mr. Examiner, --

22 MR. CLENNON: I would also note that Staff may

1 file additional testimony concerning this testimony  
2 presented by this witness today if it feels that it  
3 is appropriate for the Commission to have this  
4 information, or have additional information; I'm  
5 sorry.

6 MR. SPRINGER: Mr. Examiner, the Company has  
7 no objection to the on-the-record data request. If  
8 I understand the request, the request is for any  
9 orders or stipulations entered into in the other  
10 states referenced, and those will be provided.

11 If other motions regarding testimony or  
12 so forth are ultimately presented, we will respond  
13 accordingly at that time, and, as I indicated, the  
14 Company believes it has adequately responded to all  
15 discovery in this proceeding.

16 MR. CLENNON: Your Honor, I believe  
17 Mr. Fitzhenry's list was far from being inclusive  
18 of all the things necessary to provide the  
19 information. The Staff data request is clear. The  
20 instructions are clear. The Company should be  
21 required to provide the Staff with this information  
22 in Staff Data Request 1.02 and nothing short of it.

1           EXAMINER SHOWTIS: Well, I have no independent  
2 knowledge of what has been provided, but I think  
3 counsel for Staff should talk with counsel for IAWC  
4 to determine what has been provided, and I haven't  
5 heard any objection to providing requested  
6 information, so I don't really have anything to  
7 rule on at this time other than to direct IAWC to  
8 comply with that data request, if they have not  
9 done so.

10          MR. CLENNON: Very good.

11          MR. FITZHENRY: Just an additional, of course  
12 that information would be needed as soon as  
13 practical in light of the briefing schedule which  
14 needs to be resolved by the end of tomorrow, and so  
15 perhaps the Company could commit to provide that  
16 information by some time -- well, early next week.  
17 I don't know what's all involved in the copying  
18 processes.

19          MR. SPRINGER: I'm not sure what is being  
20 requested here. The data request reference was  
21 responded to quite some time ago.

22          MR. FITZHENRY: But the on-the-record data

1 request that the Hearing Examiner has said is  
2 appropriate calls for the orders that have been  
3 entered in these other jurisdictions and any  
4 stipulations reached between the companies in those  
5 jurisdictions and the staff or any other parties  
6 about these matters, and that's the information  
7 that we'd like to have as soon as possible.

8 MR. SPRINGER: That can be provided I  
9 understand by tomorrow.

10 MR. FITZHENRY: Well, that's too early.

11 (Laughter)

12 I have to carry that back.

13 (Laughter)

14 Thank you. And that would be for any  
15 updates too. If there would be a stipulation that  
16 would come out of this or another order between now  
17 and at the end of the briefing stage, that was  
18 intended to be part of my on-the-record data  
19 request, Mr. Showtis.

20 EXAMINER SHOWTIS: Okay.

21 MR. SPRINGER: Okay. Can I hear that part of  
22 it again? I guess I'd just like to make sure I've

1 got -- all orders, stipulations, or revised --

2 MR. FITZHENRY: You know, or new stipulations  
3 or orders not entered that will be entered in these  
4 jurisdictions that have been --

5 MR. SPRINGER: Okay.

6 MR. FITZHENRY: -- referenced by Mr. Hartnett  
7 in his examination here this morning.

8 MR. SPRINGER: Very well. That can be done.

9 MR. FITZHENRY: Thank you.

10 EXAMINER SHOWTIS: And just so I -- just to go  
11 back to one last matter, there's a stipulation with  
12 staff in Arizona regarding certain matters. Is  
13 that correct?

14 THE WITNESS: That's correct.

15 EXAMINER SHOWTIS: Were there other parties  
16 besides staff in that proceeding?

17 THE WITNESS: There is. I forget the actual  
18 name of the consumer advocate group. The acronym  
19 is RUCO.

20 EXAMINER SHOWTIS: RUCO?

21 THE WITNESS: RUCO, R-U-C-O, and they have not  
22 stipulated.



1 (Whereupon at this point in  
2 the proceedings an  
3 off-the-record discussion  
4 transpired.)

5 EXAMINER SHOWTIS: We'll put the next witness  
6 on.

7 MR. SPRINGER: Our next witness will be  
8 Mr. Gloriod.

9 Before we proceed with Mr. Gloriod, I'd  
10 like to indicate that one portion of his exhibits  
11 was placed under seal based on rulings at a prior  
12 hearing, and that is attachments to a contract  
13 which is Exhibit 1.1 of Mr. Gloriod's presentation.

14 We have the public redacted version of  
15 the attachments on the e-Docket, and I'm planning  
16 to seek admission of that version of the exhibits  
17 as attachments to Exhibit 1.1. The confidential  
18 material, which was made confidential pursuant to a  
19 motion of Citizens Utilities Company, has been  
20 marked as Exhibit 1.2, and Ms. Conti will address  
21 that exhibit.

22 MS. CONTI: I think I have a minor

1 clarification. I think Mr. Gloriod does have a 1.2  
2 of his own. When it was distributed, it was  
3 distributed in sealed envelopes after the  
4 Examiner's rulings, and it's labeled just  
5 Confidential and Proprietary Excerpts from Exhibit  
6 1.1 Attachments, and all the parties who have  
7 signed the proprietary agreement obviously have it.  
8 The Staff and the Examiner have it, and I guess  
9 that's all we would be moving admission of at this  
10 point.

11 EXAMINER SHOWTIS: Okay. I think we should  
12 identify it with some sort of --

13 MS. CONTI: If you'd like to have another  
14 number or something, we can give it one.

15 EXAMINER SHOWTIS: I think we should, and the  
16 Reporter can mark the envelope.

17 MR. CLENNON: Can I ask a question for  
18 clarification?

19 EXAMINER SHOWTIS: Yes.

20 MR. CLENNON: Is the redacted version as well  
21 as the unredacted version going into the record?

22 MS. CONTI: The redacted version definitely,

1     and the unredacted is just the excerpts, the  
2     particular pages.

3             EXAMINER SHOWTIS: The redacted version I  
4     believe would be on e-Docket, and it would be part  
5     of the public record. The confidential portions  
6     are in the envelope, and we'll mark those  
7     separately.

8             MR. CLENNON: Very good.

9             EXAMINER SHOWTIS: And those will be,  
10    obviously, afforded proprietary treatment.

11            Let's go off the record.

12                               (Whereupon at this point in  
13                               the proceedings an  
14                               off-the-record discussion  
15                               transpired, during which  
16                               time Joint Applicants'  
17                               Exhibit 11 was marked for  
18                               identification.)

19            MR. SPRINGER: Again, to clarify our  
20    off-the-record discussion, I believe I made  
21    reference to confidential material being designated  
22    as Exhibit 1.2. That confidential material will be

1 designated as Joint Applicants' Exhibit 11 based on  
2 our off-the-record discussion, and I also have  
3 become aware that there is an Exhibit 1.2 to  
4 Mr. Gloriod's testimony which is a separate piece  
5 of material. So Joint Applicants' Exhibit 11 is  
6 the confidential material I referred to, and with  
7 that, we're ready to proceed with the direct  
8 examination.

9 TERRY L. GLORIOD  
10 called as a witness on behalf of the Joint  
11 Applicants, having been first duly sworn, was  
12 examined and testified as follows:

13 DIRECT EXAMINATION

14 BY MR. SPRINGER:

15 Q. Please state your name and business  
16 address.

17 THE WITNESS:

18 A. Terry Gloriod, 300 North Water Works  
19 Boulevard, Belleville, Illinois 62223.

20 Q. And, Mr. Gloriod, by whom are you  
21 employed?

22 A. Illinois-American Water Company.

1           Q.     And what is your position with that  
2 company?

3           A.     President.

4           Q.     And have you prepared testimony for  
5 purposes of this proceeding?

6           A.     Yes.

7           Q.     I show you what's been marked for  
8 identification as IAWC Exhibit 1.0 and ask if that  
9 is a copy of direct testimony that you prepared for  
10 this case?

11          A.     Yes.

12          Q.     And in the course of that testimony do  
13 you sponsor Exhibit 1.1 which is the Asset and  
14 Stock Purchase Agreement?

15          A.     Yes.

16          Q.     And do you also sponsor Exhibit 1.2  
17 which is advantages offered by IAWC to the CUCI  
18 division?

19          A.     Yes.

20          Q.     I now show you what's been marked for  
21 identification as Exhibit 1.0R and ask if that is a  
22 copy of rebuttal testimony that you prepared for

1       this proceeding?

2           A.     Yes.

3           Q.     Have you also prepared for this  
4       proceeding Exhibit 1.0SR which is your surrebuttal  
5       testimony?

6           A.     Yes.

7           Q.     And in that testimony do you sponsor  
8       Exhibit 1.3SR which is a First Amendment to the  
9       Asset and Stock Purchase Agreement?

10          A.     Yes.

11          Q.     Is there attached to Exhibit 1.1, the  
12       Asset and Stock Purchase Agreement, a public  
13       redacted version of certain attachments to that  
14       agreement?

15          A.     Yes.

16          Q.     Has there also been marked for  
17       identification Joint Applicants' Exhibit 11 which  
18       contains the same attachments in an unredacted  
19       form?

20          A.     Yes.

21          Q.     And it's your understanding that Joint  
22       Applicants' Exhibit 11 has been placed under seal

1 in this proceeding. Is that correct?

2 A. Yes, that's correct.

3 Q. Is the information contained in your  
4 testimony and exhibits true and correct to the best  
5 of your knowledge?

6 A. Yes, it is.

7 MR. SPRINGER: At this time, Mr. Examiner, I  
8 would ask for admission into evidence of  
9 Mr. Gloriod's direct testimony, IAWC Exhibit 1.0,  
10 and Exhibits 1.1 and 1.2 which he sponsors in that  
11 testimony, Exhibit 1.1 containing the public  
12 redacted version of the attachments to the Asset  
13 and Stock Purchase Agreement, Exhibit 1.0R,  
14 Mr. Gloriod's rebuttal testimony, Mr. Gloriod's  
15 surrebuttal testimony which is Exhibit 1.0SR, and  
16 Exhibit 1.3SR which he sponsors in that testimony.

17 MS. CONTI: And I would move for admission  
18 into evidence in confidential and proprietary  
19 status Joint Applicants' Exhibit Number 11.

20 EXAMINER SHOWTIS: Are there any objections?

21 MR. FITZHENRY: No.

22 EXAMINER SHOWTIS: IAWC Exhibits 1.0, 1.1,

1 1.2, 1.0R, 1.0SR, 1.3SR, and Joint Applicants'  
2 Proprietary Exhibit 11 are admitted.  
3 (Whereupon IAWC Exhibits  
4 1.0, 1.1, 1.2, 1.0R, 1.0SR,  
5 1.3SR, and Joint Applicants'  
6 Proprietary 11 were received  
7 into evidence.)

8 MR. SPRINGER: Thank you.

9 Mr. Gloriod is available for  
10 cross-examination.

11 EXAMINER SHOWTIS: Mr. Fitzhenry.

12 MR. FITZHENRY: Sure.

13 CROSS EXAMINATION

14 BY MR. FITZHENRY:

15 Q. Good morning Mr. Gloriod.

16 A. Good morning.

17 Q. As President of IAWC, you verified the  
18 Amended Verified Application. Correct?

19 A. Correct.

20 Q. Do you have a copy of that before you?

21 A. No. I'll get one.

22 (Whereupon the witness was

1 provided with said document  
2 by Mr. Springer.)

3 I have it.

4 Q. All right. Thank you. Would you turn  
5 to paragraph 32 of that filing? Is it correct that  
6 it states, in part, that rate orders issued for the  
7 combined company, ratepayers would be assigned at  
8 least 10 percent of the demonstrated savings?

9 A. Yes.

10 Q. And the combined company is the combined  
11 CUCI and IAWC companies?

12 A. Correct.

13 Q. Now is it my understanding that after  
14 the acquisition, IAWC contemplates maintaining  
15 separate rates for CUCI from IAWC?

16 A. We've not really done a determination of  
17 that. There's no definitive plan one way or the  
18 other at this stage.

19 Q. Well, explain to me then what's  
20 represented here in paragraph 32. When you talk  
21 about rate orders, I assume that means two separate  
22 rate orders and how that 10 percent of the

1 demonstrated savings would be assigned in that way.

2 A. I think the plural, rate orders, refers  
3 to subsequent rate orders occurring over time after  
4 the transaction is closed.

5 Q. Okay. Thank you.

6 Now I'd like you to turn to paragraph 34  
7 of the Amended Verified Application and  
8 particularly subparagraph (b). As I read that, it  
9 indicates that in support for the Savings Sharing  
10 Proposal and the benefits from the acquisition, it  
11 is suggested the financial strength of the American  
12 Water Works system will assure that both IAWC and  
13 CUCI will have enhanced ability to attract capital  
14 at competitive rates. Have I fairly characterized  
15 that portion of the application?

16 A. Yes.

17 Q. Does AWW, or American Water Works, have  
18 the ability to attract capital to all of its  
19 operating subsidiaries?

20 A. Yes.

21 Q. And, hypothetically, had American Water  
22 Works purchased CUCI directly, would CUCI be the

1 beneficiary of American Water Works' ability to  
2 attract capital or to attract capital at favorable  
3 rates?

4 A. I would assume so.

5 Q. Now I'd like to ask a couple questions  
6 about the Asset and Stock Purchase Agreement, and I  
7 don't think that anything that I would ask is of a  
8 confidential nature, and if you believe so, let me  
9 know, but if you turn to - this is attached to your  
10 direct testimony - to page 41 or Section 5.9, I'd  
11 like to ask you a couple questions about this  
12 agreement.

13 A. I have it.

14 Q. Are you familiar with these provisions,  
15 Mr. Gloriod?

16 A. I have read them.

17 Q. The CUCI union employees, what will  
18 happen to them after the acquisition?

19 A. Since this is an asset purchase  
20 agreement and since we intend to retain as  
21 employees a significant number of those currently  
22 represented by the union, we will be, in a sense,

1 sitting down to negotiate terms of the continuing  
2 marketing agreement with that group.

3 Q. And so there are in existence collective  
4 bargaining agreements between CUCI and the various  
5 unions that support CUCI's services and so forth?

6 A. That's correct.

7 Q. And it's currently the plans of IAWC to  
8 honor those agreements while they're still in  
9 effect?

10 A. We have taken the position that there  
11 are some provisions of those agreements that will  
12 have to be changed to account for differences in  
13 benefits and things of that nature.

14 Q. In terms of any of the reduced positions  
15 that have been discussed in this case, the 25  
16 positions or so, are any of those positions  
17 anticipated to be union employees?

18 A. Yes.

19 Q. Now I also see in this Section 5.91 that  
20 IAWC and CUCI negotiated that there would be a  
21 minimum level of hourly and salaried employees kept  
22 on after the acquisition. Is that right?

1           A.     That's correct.

2           Q.     And that number is 250.

3           A.     Yes.

4           Q.     And by virtue of -- well, let me ask it  
5     this way. Some of the 25 positions that have been  
6     indicated that will be reduced as a result of that  
7     acquisition, those are -- some of those are hourly  
8     and salaried employees?

9           A.     Only a few, yes.

10          Q.     So even if you thought after the  
11     acquisition you could reduce -- let me ask this  
12     question. How many of the 25 positions that you  
13     said are a few are hourly and salaried employees?

14          A.     Subject to check, I think only three are  
15     hourly employees who would be represented by the  
16     bargaining agreement.

17          Q.     And so do I understand this -- I'm  
18     sorry. Could you say that again?

19          A.     I think only three.

20          Q.     Three that are --

21          A.     That are hourly.

22          Q.     Okay. So even after the acquisition, if

1     you thought more of them should be eliminated,  
2     those positions, you would be barred by virtue of  
3     the provision here that requires you to keep at  
4     least 250 of those employees.

5           A.     Correct.

6           Q.     Let me ask you to turn to page 8 of your  
7     direct testimony, and the question on line 12 asks  
8     about the considerations which support the adoption  
9     of the Savings Sharing Proposal, and as part of  
10    your answer you suggest that the combined companies  
11    will be able to more effectively pursue acquisition  
12    of and to manage and obtain small underfunded water  
13    and wastewater systems. Correct?

14          A.     Correct.

15          Q.     And then later, I believe it's in your  
16    rebuttal or surrebuttal testimony, you talk about  
17    the five smaller utility systems that could be  
18    assimilated by IAWC in the event the acquisition is  
19    approved in this proceeding?

20          A.     Yes.

21          Q.     Those are the five smaller water utility  
22    systems that I spoke with Mr. Townsley about

1 yesterday?

2 A. Yes.

3 Q. Now, first of all, tell me why it is  
4 that IAWC's possible acquisition -- strike that.

5 Would IAWC be able to acquire these  
6 smaller water systems absent its acquisition of  
7 CUCI?

8 A. We would, and it would be more a  
9 difficult proposition. We've investigated the  
10 acquisition of these systems in the past. Due to  
11 the geographic distance that our current operating  
12 centers are away from these systems, our cost of  
13 operations there would be higher than if we were  
14 geographically closer, and so we have just not been  
15 able to structure a transaction that is attractive  
16 to buyer and seller.

17 Q. And if the acquisition of CUCI is  
18 approved, because of the geographical proximity you  
19 believe there might be a better chance of acquiring  
20 these five smaller water utility systems?

21 A. Yes, I do. I think our operating costs  
22 would be much more efficient if we are

1 geographically closer to these systems, and the  
2 opportunity would be better than otherwise.

3 Q. Have you attempted in the context of  
4 this proceeding to quantify the savings, if you  
5 will, that could be acquired by virtue of CUCI's  
6 acquisition of these small water utility systems as  
7 part of the overall IAWC group?

8 A. No, we have not.

9 Q. I guess I've heard this mentioned before  
10 that IAWC is the largest investor-owned water  
11 utility in the State of Illinois. Correct?

12 A. Correct.

13 Q. And that CUCI is the third largest?

14 A. I've heard that in this hearing. I  
15 don't know if that's correct.

16 Q. Okay. And Consumers is the second  
17 largest?

18 A. I think that's correct.

19 Q. In terms of geographical proximity as of  
20 today, do you know whether or not Consumers is  
21 closer to these five smaller water systems than  
22 IAWC?

1           A.     No, I don't know that.

2           Q.     If I understand what you said just a few  
3 minutes ago, the fact that your acquisition of CUCI  
4 would put you closer geographically to these five  
5 smaller water systems, would that give you an  
6 advantage over Consumers if they are now further  
7 away from these five smaller water systems, all  
8 things being equal?

9           A.     I don't know that. I don't know that it  
10 would or would not.

11          Q.     Well, I guess I understood you to tell  
12 me that geographical proximity made a difference in  
13 terms of making this a more economic acquisition,  
14 the five smaller water utility systems. Wouldn't  
15 that hold true for Consumers?

16          A.     I would suspect that it would, but I  
17 think the geographic distance is relative. If  
18 you're close enough to be able to service a new  
19 territory, then the fact that someone else may be  
20 closer may, in fact, not have anything to do with  
21 who has a greater advantage on acquiring. What I  
22 said was where Illinois-American is today a

1 stand-alone without Citizens Utilities, the  
2 distance that we would have to go to service those  
3 smaller utilities has an impact on what kind of  
4 arrangement we could arrive at for possible  
5 purchase.

6 Q. Okay.

7 A. Once we are combined with Citizens  
8 Utilities, the distance change is great enough that  
9 we have a greater advantage of possibly making a  
10 transaction come about.

11 Q. Okay.

12 Let me ask you to turn to your rebuttal  
13 testimony, page 3, and I have some just general  
14 questions about the SSP, which you have indicated  
15 that you understand how it's intended to operate.  
16 Correct?

17 A. Okay.

18 Q. Am I correct in understanding that in  
19 order to implement the SSP, there will first be  
20 determined a cost of service study for the combined  
21 companies?

22 A. Could you again refer me to where you

1 are in my rebuttal testimony?

2 Q. Well, I know that you discuss elements  
3 of the SSP at page 3, but I know that you also  
4 talked about the SSP in your direct testimony.  
5 It's just a general question about how it works.

6 A. Okay.

7 Q. Maybe a page reference wasn't necessary.  
8 So, again, my question is, in order to implement  
9 the shared savings proposal, IAWC will first  
10 determine a cost of service for the combined  
11 companies.

12 A. Yes.

13 Q. And the cost-of-service study that would  
14 be performed for the combined companies would not  
15 include the acquisition adjustment.

16 A. I'm not sure. I'm not sure what you're  
17 asking me. I mean we believe in our Savings  
18 Sharing Proposal that the acquisition adjustment  
19 revenue requirement is a portion of the cost of  
20 service.

21 Q. In the beginning of the process though  
22 you do not include the acquisition adjustment as

1 part of what you determine to be the cost of  
2 service for the combined companies.

3 A. You're talking about the steps we would  
4 go through?

5 Q. Yes.

6 A. Okay. I will accept that.

7 Q. In this process, is there ever an  
8 examination of a cost of service for each of the  
9 companies on a stand-alone basis?

10 A. We will make -- well, in the context of  
11 a future rate proceeding, what we have said that we  
12 will do, we'll be able to identify the difference  
13 between current cost of service and the cost of the  
14 stand-alone utility. That is, in fact, how we  
15 would go about demonstrating the savings that would  
16 result from the transaction.

17 Q. Okay. Let me just be sure I'm  
18 understanding you, Mr. Gloriod. I understand and  
19 people have represented that there will be a  
20 cost-of-service study, just like probably any other  
21 rate case, on a combined company basis. Correct?

22 A. Okay. Yes.

1           Q.     And during, you know, some period of  
2     time you will be keeping track of records and so  
3     forth to show that there are demonstrated savings.  
4     Is that correct?

5           A.     Correct.

6           Q.     And then you need to, you know, prove up  
7     those demonstrated savings. Will you also  
8     construct a cost-of-service study for CUCI, even  
9     though it no longer exists on a stand-alone basis,  
10    and also a cost-of-service study for IAWC on a  
11    stand-alone basis?

12          A.     We have stated that we will maintain our  
13    books and records in a way that our district  
14    service areas will be separately identifiable as to  
15    costs. To the extent that the former Citizens  
16    Utility Company is a distinct rate area of  
17    Illinois- American, it would be identifiable. Is  
18    that the question you're asking me?

19          Q.     Well, I understand that you're going to  
20    maintain books and records, but will the end result  
21    of the maintaining of these books and records be  
22    the same thing as what we all know as a traditional

1 cost-of-service study for that CUCI service area?

2 Is that what you intend?

3 A. That's my intent, yes.

4 Q. Let me ask you to turn to page 5 your  
5 rebuttal testimony. You indicate that if the  
6 savings plan, at lines 1 through 4, by the way, if  
7 the savings plan or recovery of the acquisition  
8 adjustment is not approved, the Company would be  
9 left in an impaired financial condition. Correct?

10 A. Correct.

11 Q. Under the agreement that IAWC has with  
12 CUCI, if the Commission were to enter an order that  
13 would not allow the Company to recover the  
14 acquisition adjustment, would the Company have the  
15 option to back out of the transaction?

16 A. You're asking me a legal question that  
17 really I would -- all I can say is we would have to  
18 explore our options at that time based on the  
19 provisions of the purchase agreement and based on  
20 the precise wording of the Commission order at that  
21 time. I can't forecast what we would do.

22 Q. Well, okay, because in Mr. Showtis'

1 examination of Mr. Hartnett, I recall that he asked  
2 a question, you know, if the Commission were to  
3 impose I think a financial condition that was  
4 different than what was contemplated here, that  
5 Mr. Hartnett as treasurer for American Water Works  
6 couldn't support the acquisition. At least that's  
7 what I thought he said. Is that your  
8 understanding?

9 A. Mr. Hartnett talked about specific  
10 economic structure that was a part of his entire  
11 analysis in arriving at an appropriate purchase  
12 price. What I understood him to say was if the  
13 Commission would issue an order that would  
14 materially impact the economics of the deal, that  
15 it wouldn't be the same -- that it would change the  
16 analysis that he had done.

17 Q. Right. That's what I understand too,  
18 and so, again, I hope this is a fair question. If,  
19 hypothetically, the Commission said, you know, we  
20 basically approve the acquisition adjustment and  
21 the shared savings plan; however, for these reasons  
22 we believe there ought to be a rate freeze in the

1 CUCI service territory for five years, in your  
2 judgment that would be a financial impediment.  
3 Correct? Or do you know?

4 A. It would. I think it would.

5 Q. And based on everything that you know  
6 now and the Company's position and American Water  
7 Works' position, that would negate the transaction.  
8 Correct?

9 A. I can't go that far.

10 Q. Okay.

11 A. I mean you've asked me about some middle  
12 ground here that I haven't done any analysis on.

13 EXAMINER SHOWTIS: I guess my question would  
14 be, it's not whether the purchase would be  
15 consummated, but whether American Water Works would  
16 have the ability to decide that it doesn't want to  
17 go through with the asset purchase if the  
18 Commission's ratemaking treatment of the  
19 acquisition adjustment and allocation of savings is  
20 found to be unacceptable to AWW. I'm just trying  
21 to get an answer as to whether AWW would be able  
22 to, for want of a better term, get out of the

1 purchase if the ratemaking treatment of the  
2 acquisition adjustment and savings is found to be  
3 unacceptable.

4 THE WITNESS: There are provisions in the  
5 purchase agreement that relate to events that might  
6 occur that would allow parties to review the deal  
7 as to whether it should or if they both desired it  
8 to go forward. The hypothesis that has been  
9 presented is one that might be subject to those  
10 provisions in the agreement. It might cause the  
11 parties to change, change the agreement or to do  
12 away with it, but whether, in fact, that would  
13 occur would be dependent on a legal analysis at the  
14 time, comparing the exact order of the Commission,  
15 if you will, against the terms of the agreement and  
16 reaching a decision. I can't sit here today and  
17 forecast what would or would not occur or what the  
18 legal opportunities and rights are of the parties  
19 based on a hypothesis.

20 EXAMINER SHOWTIS: But just to ask an  
21 alternative question, the asset purchase agreement  
22 does not provide that -- or does it? That the SSP

1 in its entirety has to be approved before AWW would  
2 be obligated to consummate the purchase?

3 THE WITNESS: No, there's no direct language  
4 like that in the agreement.

5 EXAMINER SHOWTIS: Go ahead.

6 MR. FITZHENRY: Thank you.

7 Q. Could you turn to page 10 of your  
8 rebuttal testimony? You indicate there in response  
9 to the question that begins on line 7 that  
10 regulatory lag does not offer a reasonable  
11 opportunity for shareholders to recover a  
12 meaningful portion of their investment to produce  
13 savings in this case, and I want to ask a couple  
14 questions about that statement, Mr. Gloriod.

15 If the acquisition is approved and IAWC  
16 undertakes the steps it has described in this  
17 proceeding, eliminating positions and doing those  
18 kind of things, that from that point in time to the  
19 time of the next rate case, that would be  
20 regulatory lag, and in that period of time  
21 shareholders of the Company would benefit directly.  
22 Correct?

1           A.     Correct.

2           Q.     And I understand your point is that that  
3     period of time, whatever it is, would not be long  
4     enough to allow the Company to capture the  
5     acquisition adjustment in its entirety.  Correct?

6           A.     That's correct.

7           Q.     Now currently IAWC is in a rate case,  
8     00-0340.  Right?

9           A.     Yes.

10          Q.     And you would expect the Commission  
11     order sometime this spring?

12          A.     Yes.

13          Q.     And the Company's history has been to  
14     file, since the early mid 1980s, to file a rate  
15     case every two or three years.  Correct?

16          A.     Correct.

17          Q.     Is it expected that IAWC will not file  
18     its next rate case until say 2002, 2003?  Is that  
19     what's currently planned?

20          A.     No, no.  We've recognized that there's  
21     been a significant amount of capital investment in  
22     the Citizens Utility that is not covered in current

1 rates, which might cause us to accelerate a rate  
2 filing sooner than we would have under just  
3 Illinois-American.

4 Q. Okay. You've mentioned that the CUCI  
5 rates are deficient. Correct?

6 A. Yes.

7 Q. And, first of all, how do you know that?

8 A. We know it by just examining the amount  
9 of capital investment that they have made since  
10 their last case.

11 Q. So it's your contention they're under-  
12 earning?

13 A. I would believe that they are, yes.

14 Q. There's nothing to prevent, if the  
15 acquisition goes through, from CUCI filing a rate  
16 filing the day after, correct, the day after the  
17 acquisition is approved, as a stand-alone service  
18 area? Well, let me strike that question and ask  
19 hopefully a better question.

20 I think it has been in Mr. Stafford's  
21 testimony and Mr. Ruckman's testimony that  
22 traditionally the Company, IAWC, files for a rate

1     increase or rate cases for all of its service areas  
2     at the same time.

3             A.     That's not true of the current case.

4             Q.     Well, you filed a rate case that covers  
5     the Northern Division, Eastern Division, and  
6     Southern Division, correct?

7             A.     Correct, but there's not a rate increase  
8     proposed for all tariffed districts within those  
9     divisions.

10            Q.     Okay. Well, let me -- I'm trying to  
11     understand what are your plans for CUCI and IAWC  
12     vis-a-vis a rate case if the acquisition is  
13     approved?

14            A.     Okay. I don't have a plan, but I have  
15     an expectation that we would attempt to file for  
16     rates in the former Citizens territory to bring the  
17     rates up to be current with the level of capital  
18     investments since their prior case.

19            Q.     And would you plan also bringing in the  
20     other IAWC service territories and rate areas as  
21     part of that filing?

22            A.     Well, we would examine them, but it's

1 not my expectation at this point that their rates  
2 would be deficient.

3 Q. Okay. That's what I'm trying to get to,  
4 because it has been the Company's history every two  
5 or three years for IAWC to file a rate case. You  
6 wouldn't think the day after the rate order comes  
7 in in 00-0340 that your rates are deficient, would  
8 you?

9 A. No, I would not.

10 Q. And so where I'm getting to with all  
11 this is that between the time of the acquisition  
12 and the time of the next rate case for IAWC, that  
13 regulatory lag period, IAWC will be the beneficiary  
14 of the savings that may result -- the demonstrated  
15 savings that may result and flow back to IAWC.  
16 Correct?

17 A. That's correct.

18 Q. Now let me ask you to turn to page 3 of  
19 your surrebuttal testimony, and at lines 16 through  
20 18 you say, "The only issue before the Commission  
21 is CUCI remaining as a stand-alone company versus  
22 CUCI being acquired by Illinois-American with the

1     resultant benefits that have been described."

2     Correct?

3             A.     Correct.

4             Q.     Am I correct in understanding that the  
5     projected vast majority of savings under the SSP  
6     will be realized in the CUCI service territory?

7             A.     That's correct.

8             Q.     In fact, there was a response to an IIWC  
9     data request that indicated that the projected data  
10    -- the projected demonstrated savings in the CUCI  
11    service area would be about 95.5 percent?

12            A.     I recall a data request that Mr. Ruckman  
13    responded to that may have had those percentages in  
14    it, yes.

15            Q.     And so then it's expected that 4.5  
16    percent of the demonstrated savings would flow back  
17    to current IAWC service territories and areas.

18            A.     Yes.

19            MR. FITZHENRY: Let me just check my notes  
20    here real quick.

21                    (Brief pause in the proceedings.)

22                    Thank you, sir. That's all the

1 questions I have.

2 THE WITNESS: You're welcome.

3 MR. CLENNON: I have some questions. May I

4 proceed, Your Honor?

5 EXAMINER SHOWTIS: Yes.

6 CROSS EXAMINATION

7 BY MR. CLENNON:

8 Q. Good afternoon, Mr. Gloriod.

9 A. Good afternoon.

10 Q. Do you have the Asset and Stock Purchase

11 Agreement up there with you still?

12 A. Yes, I do.

13 Q. Would you turn to page 53?

14 A. Page 53?

15 Q. Page 53, sir. I'm sorry. Yes. Are you

16 there?

17 A. Yes.

18 Q. And Article 6 is entitled Conditions

19 Precedent; Termination.

20 A. Yes.

21 Q. And paragraph 6.1.4, Required PUC and

22 Other Consents, states, and I will just read the

1 first couple of lines, and I'm not asking your  
2 opinion, by the way, as an attorney, but whether or  
3 not this says what it says. The PUC, and I'm  
4 assuming that means the Illinois Commerce  
5 Commission in this particular case?

6 A. That's correct.

7 Q. Shall have issued an order approving the  
8 transaction contemplated hereby, and such order  
9 shall not contain any restrictions or conditions  
10 other than those in effect on the date thereof or  
11 requiring that the regulatory treatment with  
12 respect to the business existence as of the date of  
13 the agreement applicable to the seller shall be  
14 continued following the transaction contemplated  
15 hereby which would have a material adverse effect  
16 or a material adverse effect on any other regulated  
17 business of parent or Illinois-American Water  
18 Company in the state in which the PUC has  
19 jurisdiction, and it goes on to say the order shall  
20 be final and unappealable, and it does go on to say  
21 a number of things. Is this the section that you  
22 were thinking of when Mr. Fitzhenry was asking you

1 those questions?

2 A. This is one of the sections.

3 Q. Sir, are you familiar with Docket  
4 01-0001 here at the Commission? It is a petition  
5 for a certificate of public convenience and  
6 necessity to provide water service to the areas and  
7 near the Village of Bolingbrook, Will and DuPage  
8 County. It was filed by Citizens Utilities  
9 Company.

10 A. I don't know that I'm familiar with the  
11 specifics of that.

12 Q. Sir, is it your understanding that this  
13 service area, if the certificate is granted, would  
14 be included in this asset transfer?

15 A. Yes.

16 Q. It will be included?

17 A. Yes.

18 Q. The customers of -- the citizens of  
19 Bolingbrook and the other certificated areas have  
20 never been part of Citizens. Is that your  
21 understanding as well?

22 A. That is my understanding.

1           Q.     And this area and the assets would be  
2 covered by the SSP. Is that true?

3           A.     Yes.

4           MR. CLENNON: I think that's all the questions  
5 I have, but if I could just check.

6           EXAMINER SHOWTIS: Okay.

7                     (Pause in the proceedings.)

8           MR. CLENNON:

9           Q.     Sir, could you turn to page 11 of your  
10 direct testimony? I'm sorry; page 10.

11          A.     Yes.

12          Q.     At the bottom of page 10 and going on to  
13 page 11 you talk about various acquisitions,  
14 including both the United Water Company of Illinois  
15 as well as Northern Illinois Water Company.

16          A.     Yes.

17          Q.     Isn't it true that one of the first  
18 things that Illinois-American Water Company did to  
19 the customers of those two utility companies was to  
20 raise their rates in a rate case?

21          A.     Yes.

22          MR. CLENNON: That's all the questions I have.

1           EXAMINER SHOWTIS: I just had a couple  
2       questions. These are clarification questions in  
3       response to some answers you provided to  
4       Mr. Fitzhenry.

5                                   EXAMINATION

6           BY EXAMINER SHOWTIS:

7           Q.     Assume for purposes of these questions  
8       that the Commission enters an order that approves  
9       the acquisition and reaches conclusions regarding  
10      the acquisition adjustment and sharing of savings  
11      that are acceptable to American Water Works, and I  
12      believe in response to Mr. Fitzhenry's questions  
13      you stated your belief that CUCI rates are  
14      deficient and that there's an under-earning  
15      situation with regard to that service territory.  
16      It's my understanding, and you can correct me if  
17      I'm wrong, that you gave some indication that there  
18      may be a rate case filed just for the CUCI service  
19      territory. Is that correct?

20          A.     That's correct.

21          Q.     And obviously it takes time to compile  
22      data necessary for the filing of a rate case, and

1 I'm not asking you to state an exact time frame,  
2 but could you tell me the approximate time frame  
3 after which the acquisition of assets is  
4 consummated in which a rate case would be filed for  
5 the CUCI service territory? And if you want to  
6 give an approximate range of years, that's fine.  
7 I'm just trying to get some indication of when  
8 there may be a filing for the CUCI service  
9 territory.

10 A. Let me answer your question this way.  
11 We would have to first determine the level of  
12 revenue deficiency that existed there, taking into  
13 account Mr. Fitzhenry's point that we would, in  
14 fact, be taking advantage of savings due to reduced  
15 employee positions and the other things that we've  
16 outlined. We would have to determine the  
17 shortfall, if you will, including those savings in  
18 existing rate levels, to determine where we were  
19 overall, and that would dictate when we had to  
20 file. It's possible, and I'm kind of going out on  
21 a limb here, that later this year, late in 2001, we  
22 may be presenting a request for rate relief for

1     that division. I think that would be the earliest,  
2     would be late this year, and then as late as say  
3     sometime in '02.

4             Q.     Okay.

5             A.     But all of that would be subject really  
6     to the final analysis of the order and scrutiny of  
7     the current revenue deficiency given that  
8     condition.

9             Q.     With regard to the existing service  
10    territories of IAWC, and Mr. Fitzhenry has pointed  
11    out that there should be a rate order shortly  
12    granting rate relief with regard to certain of  
13    those service territories.

14            A.     Correct.

15            Q.     And I believe he also pointed out that  
16    traditionally there has been about a two to  
17    three-year cycle for coming in for rate relief for  
18    most of those service territories. Is that  
19    correct?

20            A.     That's correct.

21            Q.     Do you expect that to continue? In  
22    other words, that there would probably be a rate

1 filing in another two or three years for the other  
2 service territories, or do you envision more  
3 accelerated or more delayed filings for the other  
4 service territories?

5 A. Our most recent business plan would have  
6 indicated the likelihood of a rate filing in that  
7 time frame, but clearly there's no prescriptive  
8 schedule that we're on. We really just have to  
9 examine the additions to rate base that have  
10 occurred, any changes in operating costs that are  
11 material, and we really just have to look at do we  
12 or don't we have a revenue deficiency .

13 Q. Would it be fair then to state that for  
14 the existing service territories, it's likely that  
15 there would be a rate increase filing within about  
16 two to three years, but that doesn't preclude an  
17 analysis of earnings, and rate filings may be  
18 delayed beyond that time?

19 A. I guess I wouldn't use the word likely.  
20 I would --

21 Q. I think I used it because you used it  
22 first, so if you want to take the word likely away,

1     that's fine. I'm just trying to get some  
2     understanding with regard to the other service  
3     territories.

4           A.     It wouldn't be unreasonable for us to do  
5     so given our past history, but I wouldn't -- and if  
6     I used the term likely before, then I apologize. I  
7     can't sit here today and say it's likely that we  
8     will be filing a rate case for the other operating  
9     districts in that time frame.

10          Q.     I think I just had one other question,  
11     just a clarification question with regard to your  
12     direct testimony on page 7, lines 17 through 18.  
13     You indicate that, at present, neither  
14     Illinois-American nor CUCI engages in a significant  
15     level of such activity, and you're referring I  
16     think there to non-utility activities.

17          A.     That's correct.

18          Q.     Would you just briefly describe the  
19     non-utility activities that are engaged in by  
20     Illinois-American and CUCI?

21          A.     In Illinois-American we do some service  
22     type billing for wastewater for some of our

1     municipal -- municipalities in our service  
2     districts. It's relatively minor. I'm sorry; I  
3     can't really give an example on the nature of  
4     activities that CUCI might do in that regard, but,  
5     again, it's of a minor nature.

6             EXAMINER SHOWTIS: Okay. Just a second. I  
7     think that's it. Just a minute.

8                     (Pause in the proceedings.)

9             Q.     Okay. One last question. Turn to page  
10    7 of your surrebuttal testimony. In your answer to  
11    the question on line 4 where you're addressing  
12    Mr. Gorman's control premium, you categorize it as  
13    an arbitrary definition in the first line. Would  
14    you just elaborate on what you meant by an  
15    arbitrary definition?

16            A.     I think in the context of this  
17    proceeding, the idea of a separate measure of  
18    premium or acquisition revenue requirement I  
19    consider as arbitrary. It's really I suppose my  
20    adjective. I know that the concept of a control  
21    premium is a legitimate term used in financial  
22    circles, but in the context of this proceeding and

1 in the context of our Savings Sharing Proposal, I  
2 consider it to be an arbitrary distinction.

3 Q. Well, just so I'm clear, is anything  
4 other than the acquisition adjustment -- strike  
5 that.

6 In calculating the acquisition  
7 adjustment or premium or whatever you want to  
8 characterize it as, is it your position that  
9 anything other than the manner in which it has been  
10 calculated by IAWC arbitrary?

11 A. No, and that's not what I intended. I  
12 guess we have seen -- we have seen the impact of  
13 what we proposed. We've seen the impact of what  
14 Staff proposed, and the net result of that is  
15 described in our Exhibit 3.6R, how the savings come  
16 out. This modified premium proposal where if you  
17 would essentially adopt the concept of the savings  
18 sharing but apply it to a lower base, as is  
19 suggested by Mr. Gorman, that's what I was  
20 responding to and merely saying that if we look at  
21 all three of those proposals, ours, Staff's, and  
22 this alternative, the only one of those three which

1 gets us to where we need to be is ours. I don't  
2 mean to be saying that there aren't some others out  
3 there, but I haven't seen any in the evidence other  
4 than ours.

5 Q. So when you use the term arbitrary  
6 there, if an alternative proposal by Mr. Gorman or  
7 Staff, in your words, got you to where you wanted  
8 to be, would that no longer be arbitrary?

9 A. We believe that we needed to recover the  
10 amount of acquisition revenue requirement in our  
11 proposal to comply with 7-204. I guess when we  
12 judge these other proposals in light of where we  
13 think we need to be with regard to 7-204, I guess  
14 arbitrariness here, I'm probably making a  
15 distinction between language and proposals that  
16 might sound legitimate in financial terms as  
17 distinguished from look at the result, look at  
18 where we need to be in terms of maintaining  
19 financial integrity of Illinois-American Water  
20 Company, and so in that context we can discuss all  
21 manner of financial accounting theory and how we  
22 might describe a premium, and I guess I'm saying in

1 the context of where we're trying to get to, that  
2 discussion -- maybe arbitrary is the wrong word --  
3 is sort of immaterial maybe is a better word.

4 Q. Okay.

5 A. It doesn't get us where we need to be.

6 Q. So basically you're really talking about  
7 his proposal not providing the results that are  
8 required by Illinois-American.

9 A. And what we believe are required by  
10 7-204.

11 Q. Okay.

12 A. That's the emphasis.

13 Q. Okay. Because I was just confused by  
14 your use of the word arbitrary there.

15 A. I apologize. I probably used the word  
16 incorrectly.

17 Q. No, that's fine.

18 EXAMINER SHOWTIS: That's all I have.

19 MR. SPRINGER: Mr. Examiner, we will have some  
20 brief redirect, and I would request a recess at  
21 this time.

22 EXAMINER SHOWTIS: That's fine, and we're off

1 the record.

2 (Whereupon a recess was  
3 taken.)

4 EXAMINER SHOWTIS: Back on the record for  
5 redirect.

6 MR. SPRINGER: Yes, we have some brief  
7 redirect, Mr. Examiner.

8 REDIRECT EXAMINATION

9 BY MR. SPRINGER:

10 Q. In response to questions, Mr. Gloriod, I  
11 believe you indicated that you felt there were  
12 three hourly employees included in the 25 employee  
13 total that is to be eliminated.

14 A. Correct.

15 Q. Would you care to clarify that response?

16 A. Yeah. The number of hourly employees is  
17 larger than three. The three I was referring to  
18 are three hourly employees who are represented by  
19 the bargaining unit.

20 Q. Okay.

21 You also made reference or were  
22 questioned, Mr. Gloriod, regarding a requirement in

1 the contract that offers be made to 250 employees.

2 Do you recall those questions?

3 A. Correct.

4 Q. Would you care to comment on that 250  
5 employee requirement?

6 A. I just wanted to clarify that that 250  
7 requirement is applicable to all of the Citizens  
8 properties. It's not an Illinois limit. It's  
9 applicable throughout, and that 250 number, since  
10 it is applicable to the entire six states involved,  
11 would not necessarily limit further reductions in  
12 Citizens Utilities of Illinois.

13 Q. So there could be further reductions  
14 beyond the 25 currently anticipated.

15 A. Possible, yes.

16 Q. You also were questioned with regard to  
17 whether one of the first things done in connection  
18 with the acquisitions by Illinois-American of  
19 Northern Illinois Water Company and United Water of  
20 Illinois was to raise rates. Would you care to  
21 comment on your response to that question?

22 A. I gave a quick yes, and I guess I just

1 want to elaborate on that.

2 In the case of the former Northern  
3 Illinois Water District, they would have -- under  
4 their schedule would have been in for rates  
5 probably a year earlier than that district is  
6 included currently, and so there was a coincidental  
7 time frame, if you will, that brought about their  
8 inclusion in our current rates.

9 The United Water District in Lincoln is  
10 not in our current case. We have not increased nor  
11 propose to increase rates for that district in our  
12 current case.

13 MR. SPRINGER: Thank you. That's all the  
14 questions I have.

15 MR. FITZHENRY: Just a couple of follow-up.

16 RE CROSS EXAMINATION

17 BY MR. FITZHENRY:

18 Q. In the CUCI service area, how many  
19 employees are salaried employees?

20 A. Currently?

21 Q. Currently.

22 A. I don't know.

1           Q.     And the same question as to how many are  
2     hourly employees.

3           A.     I'm sorry. I don't know.

4           MR. FITZHENRY: All right. Thank you. That's  
5     it.

6           EXAMINER SHOWTIS: You may step down,  
7     Mr. Gloriod.

8           THE WITNESS: Thank you.

9                                 (Witness excused.)

10          EXAMINER SHOWTIS: Why don't we at least get  
11     Mr. Stafford on to identify his testimony, and then  
12     we'll break for about ten minutes or so.

13          MR. SPRINGER: That's fine. Our next witness  
14     is Mr. Stafford.

15                                 RONALD D. STAFFORD  
16     called as a witness on behalf of Joint Applicants,  
17     having been first duly sworn, was examined and  
18     testified as follows:

19                                 DIRECT EXAMINATION

20          BY MR. SPRINGER:

21          Q.     Please state your name and business  
22     address.

1 THE WITNESS:

2 A. Ronald D. Stafford, 300 North Water  
3 Works Drive, Belleville, Illinois 62223.

4 Q. And, Mr. Stafford, by whom are you  
5 employed?

6 A. Illinois-American Water Company.

7 Q. And what's your position with that  
8 Company?

9 A. Director of Rates and Revenue.

10 Q. Have you prepared testimony and exhibits  
11 for purposes of this proceeding, Mr. Stafford?

12 A. Yes, I have.

13 Q. I show you what's been marked for  
14 identification as Exhibit 3.0. Is that direct  
15 testimony which you prepared for purposes of this  
16 case?

17 A. Yes, it is.

18 Q. And in the course of that testimony do  
19 you sponsor Exhibits 3.1, 3.2, 3.3, 3.4, and 3.5?

20 A. Yes, I do.

21 Q. I also show you what's been marked as  
22 IAWC Exhibit 3.0R and ask if that is rebuttal

1 testimony that you've prepared for purposes of this  
2 case?

3 A. Yes, it is.

4 Q. And in the course of that testimony do  
5 you sponsor Exhibit 3.1R, 3.5R, and 3.6R?

6 A. That's correct.

7 Q. And did you also prepare surrebuttal  
8 testimony marked as Exhibit 3.0SR?

9 A. Yes, I did.

10 Q. And are the testimonies and exhibits  
11 that you prepared true and correct to the best of  
12 your knowledge?

13 A. Yes, they are.

14 MR. SPRINGER: At this time, Mr. Examiner, I'd  
15 ask for admission of Mr. Stafford's direct  
16 testimony, IAWC Exhibit 3.0, the exhibits sponsored  
17 in that testimony, 3.1 through 3.5 inclusive,  
18 Mr. Stafford's rebuttal testimony, 3.0R, the  
19 exhibits sponsored in that testimony, 3.1R, 3.5R  
20 and 3.6R, and Mr. Stafford's surrebuttal testimony,  
21 3.0SR.

22 EXAMINER SHOWTIS: Are there any objections?

1 Those exhibits are admitted into evidence.

2 (Whereupon IAWC Exhibits  
3 3.0, 3.1, 3.2, 3.3, 3.4,  
4 3.5, 3.0R, 3.1R, 3.5R, 3.6R,  
5 and 3.0SR were received into  
6 evidence.)

7 MR. SPRINGER: Thank you.

8 Mr. Stafford is available for  
9 cross-examination.

10 MS. VON QUALEN: May I?

11 EXAMINER SHOWTIS: You may.

12 CROSS EXAMINATION

13 BY MS. VON QUALEN:

14 Q. Good afternoon, Mr. Stafford.

15 A. Good afternoon.

16 Q. Is it correct, Mr. Stafford, that you  
17 believe that management can be viewed as a  
18 representative of shareholders and customers?

19 A. Yes, I believe that to be correct.

20 Q. You do agree, do you not, that the  
21 customers of Illinois-American do not participate  
22 in the selection of Illinois American's directors

1 and officers?

2 A. That's correct. I agree with that.

3 Q. You responded to Staff Data Request TQS  
4 1.10 by indicating that Illinois-American will be  
5 purchasing Citizens' entire water and wastewater  
6 systems. Does that reflect your position?

7 A. Illinois-American would be acquiring  
8 Citizens Utilities Company of Illinois' entire  
9 water and wastewater systems.

10 Q. Thank you.

11 Do you agree that Citizens' water and  
12 wastewater systems in Illinois are composed of many  
13 individual components?

14 A. Could you clarify what you mean by the  
15 word components?

16 Q. Sure; service lines and general  
17 structure of the water company.

18 A. Well, there certainly are a number of  
19 individual service lines within the assets that we  
20 will be acquiring if the acquisition is approved.  
21 I would agree with that.

22 Q. Thank you.

1                   And you would also agree, would you not,  
2     that on the day of the completion of the merger or  
3     when the transaction is completed, no single  
4     service line will be physically larger than it was  
5     prior to the completion of the merger?

6           A.     I would clarify first by saying this is  
7     an asset acquisition rather than a merger. At the  
8     time of closing of the asset acquisition, I would  
9     agree with your comment.

10          Q.     You're familiar with the Commission  
11     order in Consumers Illinois Water Company Docket  
12     88-0045?

13          A.     At the moment I don't recall that  
14     specific order. I may be -- I may have reviewed  
15     it, but at the moment I don't recall.

16          Q.     Are you aware whether or not the  
17     Commission found in that order that Consumers  
18     restored a failing utility to a healthy financial  
19     and operating condition?

20          A.     I recall an order referenced. I don't  
21     recall the docket number where Citizens restored an  
22     ailing utility to good financial health, yes.

1           Q.     In this proceeding you are not  
2     testifying that Citizens is a failing utility, are  
3     you?

4           A.     No, I am not.

5           Q.     You are familiar with the Virginia  
6     Corporation Commission decision involving Po River  
7     Water and Sewer Company?

8           A.     Yes, I am.

9           Q.     Are you aware that one of the reasons  
10    the Commission found that the ratepayers would  
11    benefit was because the new owner brings financial  
12    stability that its predecessors lacked?

13          A.     Do you have a specific reference in that  
14    order to the language you're referring to? I have  
15    a copy in front of me.

16          Q.     I'm sorry; I do not.

17          A.     I haven't located that specific  
18    language. If it is in the order, then I would  
19    agree with your comments, subject to check.

20          Q.     Thank you.

21                 You're not testifying that Citizens  
22    currently lacks financial stability, are you?

1           A.     I don't recall testifying specifically  
2     as to whether or not Citizens lacks financial  
3     stability currently. I don't know whether they do  
4     or do not.

5           Q.     To your knowledge, has Citizens under  
6     its current ownership been unable to pay its bills  
7     when due?

8           A.     Not to my knowledge.

9           Q.     Am I correct that you are of the opinion  
10    that as long as Illinois-American and the  
11    Commission act in accordance with the Public  
12    Utilities Act, the interests of shareholders will  
13    not conflict with the interests of customers?

14          A.     Do you have a specific reference to  
15    testimony or data requests you're referring to?

16          Q.     Yes. If you would look at your data  
17    request answer to TQS 1.32.

18                   (Brief pause in the proceedings.)

19          A.     That's correct.

20          Q.     You would agree that shareholders have  
21    an interest in larger rather than smaller profits?

22          A.     I would not necessarily agree with that

1 statement the way you phrased it. I would say that  
2 shareholders are entitled to a reasonable return on  
3 their investment that they put in facilities on  
4 behalf of customers.

5 Q. Do you disagree that shareholders have  
6 an interest in larger rather than smaller profits?

7 A. As I believe Mr. Kelleher testified  
8 yesterday, the Company's intention is to balance  
9 the interest of shareholders and customers, and he  
10 referenced at least a couple examples of that  
11 within the AWW Annual Report. To the extent that  
12 customer service is provided, shareholders want to  
13 earn a reasonable return on their investment. I  
14 guess that would be my answer.

15 MS. VON QUALEN: I'd ask that his answer be  
16 stricken as nonresponsive to my question.

17 MR. SPRINGER: I believe the question was  
18 whether Mr. Stafford disagreed with the concept  
19 that shareholders wish to earn larger profits, and  
20 I think his answer was trying to respond to the  
21 question asked.

22 MS. VON QUALEN: He may have been trying to

1     respond to the question, but I don't believe he  
2     did. I understood him to refer to other  
3     testimonies speaking about this particular  
4     transaction. My question actually simply asked if  
5     shareholders -- if he disagreed that shareholders  
6     have an interest in larger rather than smaller  
7     profits. If he doesn't have an opinion, he  
8     certainly could state that.

9           EXAMINER SHOWTIS: I think Mr. Stafford was  
10    answering the question from the perspective of IAWC  
11    and also AWW, but -- well, I guess AWW is  
12    shareholder of IAWC. Is that correct?

13           THE WITNESS: Correct.

14           EXAMINER SHOWTIS: Well, let me cut through  
15    this. As a shareholder, would AWW rather see IAWC  
16    operations result in as high a profit as possible,  
17    while also taking into account the -- well, let's  
18    leave it at that.

19           THE WITNESS: Okay. I believe that as long as  
20    the proper balance is retained between shareholders  
21    and customers, then I would generally agree that,  
22    you know, the shareholders of AWW would prefer to

1     see Illinois-American have a greater profit and  
2     provide service to its customers.

3           Q.     Thank you.

4           A.     But AWW also recognizes that  
5     Illinois-American is a regulated utility and, as  
6     such, has regulated rates and is treated as a  
7     monopoly under Illinois regulation.

8           Q.     Thank you.

9           EXAMINER SHOWTIS:   Where are you in terms of  
10    your cross of Mr. Stafford?

11          MS. VON QUALEN:   I'm just getting started.

12          EXAMINER SHOWTIS:   Okay.   Then I think we'll  
13    break, unless you have something -- if you have  
14    anything on this line --

15          MS. VON QUALEN:   Yes, I have one more  
16    question.

17          EXAMINER SHOWTIS:   Follow up this line, and  
18    then we'll break.

19          MS. VON QUALEN:

20          Q.     Would you also agree that customers have  
21    an interest in lower rather than higher rates?

22          A.     I would not necessarily agree with that

1 statement only because customers want to receive  
2 quality water service, and they want to receive  
3 that service at a reasonable price. I know of  
4 examples of customers that would pay almost any  
5 price to get quality water, so I wouldn't  
6 necessarily agree with that statement to be true.  
7 I believe the primary interest of customers is  
8 quality water service.

9 Q. And if quality service remained the  
10 same, would you agree that customers have an  
11 interest in lower rather than higher rates?

12 A. As a general proposition, I would agree  
13 that customers would prefer to pay less for the  
14 same quality of water service.

15 MS. VON QUALEN: Thank you, Mr. Stafford.

16 EXAMINER SHOWTIS: We'll take a break. We'll  
17 come back at 2:00.

18 (Whereupon lunch recess was  
19 taken until 2:00 P.M.)  
20  
21  
22

1                   A F T E R N O O N   S E S S I O N

2                                   (Whereupon the proceedings were  
3                                   hereinafter stenographically  
4                                   reported by Carla Boehl.)

5                   EXAMINER SHOWTIS: Back on the record.

6                                   CONTINUED CROSS EXAMINATION

7                   BY MS. VON QUALEN:

8                   Q. Mr. Stafford, are you familiar with the  
9                   types of documents that are typically used as evidence  
10                  in a payroll audit?

11                  A. To some extent, yes.

12                  Q. Would you agree that W2s are typically  
13                  used?

14                  A. I would agree that W2s could be used,  
15                  yes.

16                  Q. Payroll ledgers?

17                  A. Yes.

18                  Q. Payroll taxes?

19                  A. Yes.

20                  Q. Other ledgers itemizing wages, employee  
21                  insurance expense, and pension expense records?

22                  A. Yes.

1           Q. Referring to page 2 of your surrebuttal  
2 testimony, lines 19 through 21.

3           A. I have that.

4           Q. You refer there to detailed information  
5 that would be maintained by the Company to document  
6 the amount of savings, is that correct?

7           A. Yes.

8           Q. Hypothetically, if an employee is laid  
9 off in 2001 and the Company brings a rate case using  
10 2010 test year data, in order to demonstrate savings  
11 as part of the evidence to be verified for inclusion  
12 in the 2010 test year data would the Company have a W2  
13 prepared in and for 2010 for that previously laid-off  
14 employee?

15          A. Not for the year 2010, no.

16          Q. In the Company ledger supporting the 2010  
17 rate case test year, will there be entries for 2010  
18 wages, taxes, insurance, and pension expense related  
19 to the employee who was laid off in 2001?

20          A. Could I have that read back, please?

21          Q. Would you like me to repeat it or --

22          A. That would be fine.

1           Q. Referring to Company ledgers supporting  
2           the 2010 rate case test year, will there be entries  
3           for 2010 wages, taxes, insurance, and pension expense  
4           related to the employee who was laid off in 2001?

5           A. The Company would maintain ledgers that  
6           would identify the savings associated with the  
7           laid-off employee in 2010, and it would provide that  
8           type of information. The type of information  
9           maintained in that Company ledger, however, would be  
10          related to the savings within itself.

11          Q. Okay. But would it be correct that there  
12          would not actually be entries for 2010 wages?

13          A. There would be no actual wages in 2010  
14          related to that laid-off position because that  
15          laid-off position creates savings and those savings  
16          would be what would be documented in 2010.

17          Q. In what Uniform System of Account are  
18          savings recorded?

19          A. Savings can be recorded in technically  
20          any Uniform System of Account where costs would be  
21          recorded. What it would be reflective of would be  
22          lower level costs as a result of the savings than

1 would otherwise be recorded.

2 Q. But isn't it correct that there would be  
3 no journal entry that identified the savings?

4 A. I am not sure if I understand the  
5 question correctly. I will see if this is responsive  
6 to your question. We will maintain journal entries  
7 we will use as part of our documentation to support  
8 savings, journal entries recorded by Citizens  
9 documenting specific events, specific costs that would  
10 be recorded. To that extent there will be journal  
11 entries used as documentation to help support savings  
12 events.

13 Q. Isn't it true that the journal entries  
14 you are referring to will actually identify costs?

15 A. The journal entries I am referring to  
16 will be identifying costs that will in part or in  
17 whole have been eliminated as a direct result of the  
18 acquisition.

19 Q. Is your testimony that there will be  
20 journal entries identifying costs that have been  
21 eliminated in their entirety?

22 A. That could be true in some cases.

1           Q. Turning to page 5 of your surrebuttal,  
2 lines 22 through 23, you refer to the Commission  
3 routinely evaluating utility information that dates  
4 back to the 1800s and you specifically refer to  
5 utility plant records, is that correct?

6           A. That's correct.

7           Q. Are these utility plant records  
8 maintained in the Company's accounting system, kept in  
9 accordance with the Uniform System of Accounts?

10          A. Yes, they are.

11          Q. Turning back to page 3 of your  
12 surrebuttal testimony, line 3, you state that the  
13 Company will be in a position to continually assess  
14 new technology available which could have affected the  
15 savings events even absent the acquisition?

16          A. That's correct.

17          Q. What is the specific process that the  
18 Company will use to continually assess new technology?

19          A. Well, further down in my testimony on  
20 that same page I explain essentially how that process  
21 will be done. At line 10, lines 9 through 12, I say,  
22 "Changes in how similar, if not absolutely identical,

1 functions are performed by IAWC and other affiliates  
2 within the American system will provide a very  
3 reliable indication of how the changes and technology  
4 are impacting these functions."

5 And also at another location, a little  
6 bit prior up on that same page starting at line 5, I  
7 say, "To properly measure the effect of technological  
8 improvements and other exogenous factors on  
9 demonstrated savings, the Company will not only  
10 maintain a record of the functions performed  
11 previously by the eliminated position but also  
12 maintain a record of how similar functions are being  
13 performed by the post-acquisition company."

14 So, essentially, I am saying there that  
15 we will maintain a record of the process that was  
16 eliminated, the function, and measure it against  
17 similar functions performed either directly by  
18 Illinois-American or other companies within the  
19 American system. And through that identification of  
20 that process we can assess whether that process would  
21 be impacted over time through technological  
22 improvements or other exogenous factors.

1           Q. Do you know who is going to be performing  
2     that function?

3           A. I don't know specifically who will be  
4     performing that function. I expect that initially I  
5     would be performing that function.

6           Q. Do you know what level of management will  
7     have final review of the assessment?

8           A. When you use the term "assessment," are  
9     you referring to something specifically?

10          Q. To continually assess new technology?

11          A. I believe that would be done by,  
12     essentially, senior management at Illinois -American.  
13     It could depend on the nature of the function, the  
14     savings event that we are looking at, and who within  
15     Illinois-American would have the greatest expertise in  
16     measuring whether technological improvements would  
17     impact that. Certainly, the financial group within  
18     the Company would be involved because the financial  
19     group gets involved in measuring cost versus benefit  
20     analysis of technological improvements, along with  
21     other experts within the Company.

22          Q. Thank you. Further down on page 3, lines

1 22 to 23 and I think continuing on to page 4.

2 A. Yes, I have that.

3 Q. Am I correct in my understanding that as  
4 part of the continual assessment, if new regulations  
5 would require additional testing, the Company would  
6 make a determination whether a new position would have  
7 been needed by the former CUCI system?

8 A. Yes, that's what my testimony states.  
9 The Company's objective here is to measure actual  
10 savings resulting directly from the acquisition. And  
11 if making that assessment would result in additional  
12 savings in the year 2010 and the year 2020 as a  
13 result, that could be tied directly to the  
14 acquisition, then it could result in additional  
15 savings.

16 Q. So a determination regarding whether or  
17 not CUCI, an entity that had not existed as a  
18 stand-alone company for, say, 15 years, in 2015 would  
19 be made to determine if they needed a new position?

20 A. Yes.

21 Q. And then the Company would re-evaluate  
22 the effect of that change for savings demonstration

1 purposes?

2 A. Correct.

3 Q. Is it correct that Illinois-American  
4 Water Company will not prepare annual forecasts of  
5 operating costs of CUCI on a stand-alone basis?

6 A. Illinois-American would not prepare  
7 annual forecasts of all costs for CUCI on a  
8 stand-alone basis. To the extent that certain costs  
9 need to be captured on a stand-alone basis to support  
10 the Company's demonstration of savings, then those  
11 costs would be measured and forecasted as needed.

12 Q. Is it the Company's intent to keep two  
13 sets of books, one reflecting actual costs, another  
14 reflecting assumed CUCI stand-alone costs?

15 A. No.

16 Q. Would you agree that monitoring savings,  
17 including the continual assessment of how changes will  
18 affect savings, will be a complicated matter?

19 A. I have thought about that quite a bit in  
20 developing my testimony, and I don't agree that it  
21 will be a complicated matter. In fact, considering  
22 the number of savings events that the Company will be

1 capturing, I think it's in many ways an easier process  
2 than many, many of the functions the Company currently  
3 performs.

4 For example, the Company is involved in  
5 processing thousands upon thousands of invoices,  
6 writing thousands of checks, dealing with hundreds  
7 upon hundreds of employees -- we currently have over  
8 300 employees -- and we are talking here in monitoring  
9 savings of a number of saving events that I am  
10 anticipating will be 50 or less. And so I think  
11 overall the process will be much easier than many of  
12 the other functions that we routinely perform and  
13 provide in service to our customers.

14 Q. But the potential for error does exist,  
15 does it not?

16 A. Yes, I would say the potential for error  
17 does exist, as it does in measuring other costs of  
18 service when setting rates in a rate proceeding.

19 Q. You are familiar with Docket Number  
20 99-0418 which was the Illinois-American Water Company  
21 merger with Northern Illinois Water Company?

22 A. Yes, I am.

1           Q. And you are familiar with the order that  
2 was entered in that docket?

3           A. Yes, I am.

4           Q. You are also familiar with the 99-0457  
5 Illinois-American Water Company merger with United  
6 Water Company?

7           A. Yes, I am.

8           Q. And with the order entered in that  
9 docket?

10          A. Yes.

11          Q. You are aware that Illinois-American  
12 Water Company was disallowed recovery of certain costs  
13 in each of those orders?

14          A. I understand that Illinois-American was  
15 disallowed recovery of what was deemed to be  
16 transaction costs in each of those orders, and also I  
17 understand that the Northern Illinois Water Order is  
18 currently under appeal in that regard.

19          Q. And you are also familiar with the  
20 Illinois-American Water rate case that was filed on  
21 May 10 of 2000?

22          A. I am familiar with the rate case. As I

1 recall, the filing date was a little bit earlier than  
2 that but, yes, I remember.

3 Q. I could be incorrect on that. Docket  
4 Number 00-0140?

5 A. Yes.

6 Q. And you were familiar with the components  
7 of rate base that were proposed by the Company in the  
8 rate case, is that correct?

9 A. Yes, I am.

10 Q. Isn't it true that in Docket 00-0340  
11 Illinois-American Water Company included disallowed  
12 costs associated with the merger of Illinois-American  
13 and Northern Illinois Water Company?

14 A. In the Northern Illinois Water Order?

15 Q. Yes.

16 A. Yes.

17 Q. And that the costs were removed pursuant  
18 to Staff's adjustment?

19 A. Correct.

20 MS. VON QUALEN: That's all the questions I  
21 have.

22 EXAMINER SHOWTIS: Mr. Fitzhenry.

1 CROSS EXAMINATION

2 BY MR. FITZHENRY:

3 Q. Good afternoon, Mr. Stafford.

4 A. Good afternoon.

5 Q. Let me ask you to refer to Schedule 3.1  
6 attached to your direct testimony.

7 A. I have that.

8 Q. This schedule is titled "Citizens  
9 Illinois Acquisition Savings," correct?

10 A. Correct.

11 Q. Are the savings that are depicted on this  
12 schedule intended to be the savings that will accrue  
13 only to the CUCI service area?

14 A. No, they are intended to reflect  
15 estimated savings that would result from the  
16 acquisition in its entirety.

17 Q. And I believe it was you that responded  
18 to a data request where IIWC had asked you to estimate  
19 what percentage of the savings would you expect to be  
20 attributable to the CUCI area and what percentage of  
21 the savings would be attributable to the IAWC, the  
22 current service territory, and is my recollection

1 correct that the breakdown was 95.5 percent to CUCI  
2 and 4.5 percent to IAWC?

3 A. Correct.

4 Q. Now, if we go to your Schedule 3.5 and  
5 under the first column it's entitled "Synergy  
6 Savings," do you see that?

7 A. This is 3.5 of my direct testimony?

8 Q. I'm sorry, your rebuttal.

9 A. I have that schedule.

10 Q. In year one, this would be year one of  
11 the acquisition, it shows that the anticipated Synergy  
12 savings, or I guess demonstrated savings as it's also  
13 been called, would be approximately \$3,747,587?

14 A. Yes.

15 Q. And the second year the again anticipated  
16 demonstrated savings would be \$4,051,694 and so forth,  
17 correct?

18 A. Correct.

19 Q. Again going back to that percentage  
20 breakdown that we talked about, it would be fair to  
21 assume, again without actually the acquisition having  
22 taken place and going about any more detail, that the

1 savings back to IAWC in the first year would be 4.5  
2 percent of the \$3.7 million?

3 A. Correct.

4 Q. Roughly \$180,000 or so?

5 A. I agree with that.

6 Q. And we could look at year two and based  
7 on the Company's proposal assume that 4.5 percent of  
8 the year two savings would be the savings that would  
9 be anticipated to flow back to IAWC?

10 A. Yes.

11 Q. Now, you talk a little bit about the  
12 Shared Savings Plan in your testimonies, correct?

13 A. Correct.

14 Q. Know a little bit about that?

15 A. Yes.

16 Q. In your response to one of the Staff data  
17 requests, MHE-030 you make a statement there that I  
18 would like to ask you a question about.

19 A. I have that.

20 Q. I don't have it right here but I remember  
21 in my notes you indicate that the determination of an  
22 actual amount of demonstrated savings in years outside

1       the test year would only be performed in order to  
2       financially measure the change in such savings  
3       properly allocable to ratepayers. That's in the first  
4       part of that data request answer.

5               A. Yes, I see that.

6               Q. In your answer there are you intending to  
7       state that the Company will sort of maintain and  
8       calculate the demonstrated savings in the years  
9       outside of a test year, I guess in between rate cases,  
10      in order to sort of, I guess, track the savings that  
11      are accruing over time?

12              A. Could I have that question read back?

13              Q. Well, I guess I am trying to ask you,  
14      what did you mean by that statement about that?

15              A. I was trying to respond to Staff's  
16      inquiry. And what I was essentially saying there was  
17      to actually go beyond the demonstration itself and  
18      assign savings by rate area. It would not necessarily  
19      be something that we would need to do unless we were  
20      going in for a rate proceeding or for some other  
21      reason need to financially measure the impact of  
22      savings by rate area and how those savings would be

1 allocated to rate areas. It is my intent to  
2 continuously, even in between rate cases, maintain a  
3 record of savings. But then to begin the next step of  
4 allocating that, I wouldn't anticipate we would be  
5 doing that unless we were going in for a rate  
6 proceeding or, as I say, measuring it for other  
7 reasons.

8 Q. But you do anticipate tracking these  
9 savings on an ongoing basis?

10 A. Yes.

11 Q. Now, somewhere in your testimony there is  
12 a representation that the Company will put forth a  
13 report every five years?

14 A. I don't recall that testimony. I know  
15 there is a reference to within five years we need to  
16 come before the Commission with a demonstration.

17 Q. Well, what will you bring to the  
18 Commission at that point in time?

19 A. Well, the original petition testimony  
20 discusses within five years providing information to  
21 the Commission for a review of savings. It's  
22 anticipated by the Company that will be done in the

1 context of the general rate proceeding, although it  
2 could be done for another reason.

3 For example, if we had -- didn't have a  
4 rate proceeding within that five-year period for some  
5 unforeseen reason -- we are committing to come to the  
6 Commission within five years -- at that time we would  
7 provide evidence of this savings and provide the  
8 substantiation that we believe is appropriate to  
9 demonstrate that those savings exist, that they are  
10 the result of the acquisition.

11 Q. And assuming, just for the sake of  
12 discussion, that the Company files a rate case in two  
13 years, is it the Company's intention to five years  
14 thereafter again make the -- prepare the sort of  
15 report that you have just outlined to the Commission  
16 and do that on an ongoing five-year basis throughout  
17 the 40-year amortization period?

18 A. No.

19 Q. That was a one shot deal?

20 A. Correct. We are committing to provide  
21 that demonstration no later than within five years  
22 after the date of this order.

1           Q. But that's one time. And then you  
2 would -- if a rate case would occur beforehand, you  
3 are not going to go ahead and provide that informati on  
4 five years after the acquisition?

5           A. No.

6           Q. Now, again going back to your response to  
7 MHE-030, you describe in there the sort of method by  
8 which the savings will be quantified. Do I understand  
9 your answer there that the Company intends to sort of  
10 quantify the savings in a way that it would structure  
11 the test year cost for expense?

12          A. Could you repeat that, please?

13          Q. You describe in the answer to the data  
14 request how you are going to go about quantifying the  
15 demonstrated savings. I think you refer in the answer  
16 to maybe the same way the Company would construct a  
17 test year cost or a test year expense. Do I read that  
18 correctly?

19          A. Yes.

20          Q. I would like you to refer to the data  
21 request IIWC proposed to you. It's 2-2. It might  
22 have been part of the third set of data requests.

1           A. I believe I have that one.

2           Q. The Data Request 2-2 starts with -- at  
3 page 7 Mr. Stafford's testimony?

4           A. That 's the one I have, yes.

5           Q. And the data request inquired of the  
6 methodology the Company was going to employ to  
7 establish demonstrated savings in future rate  
8 proceedings. And in your response, I will just read  
9 this to you, it says, "In the Company's proposed SSP  
10 acquisition savings as trended in future rate  
11 proceedings will be determined in future rate  
12 proceedings by comparing the then test year  
13 operational costs to the costs that would have existed  
14 had the Company remained a stand-alone utility." And  
15 then there is a further description about how the  
16 stand-alone costs would be determined. Did I fairly  
17 characterize that portion of your answer?

18          A. Yes.

19          Q. When you speak of costs that would have  
20 existed had the Company -- and I guess we are talking  
21 about CUCI -- remained as a stand-alone utility, would  
22 that include the costs associated with cost of service

1       for that utility?

2                   A.   Yes.

3                   Q.   Then I would like you to refer to Staff  
4       Data Request 3.17.  There was no prefix to the Staff  
5       data request.  It was one of the ones that were issued  
6       some time ago.  Do you have that?

7                   A.   I have that, yes.

8                   Q.   Now, here the data request asks following  
9       the acquisition how will the Company determine the  
10      costs of operating Citizens, whether for the purpose  
11      of a rate case or reporting to the financial community  
12      on a stand-alone basis.  And then you answer in part,  
13      "The Company will not determine the full cost of  
14      operating Citizens on a stand-alone basis after the  
15      acquisition but will determine specific savings events  
16      related to the consolidation for purposes of measuring  
17      acquisition related savings," right?

18                  A.   That's correct.

19                  Q.   Am I wrong to interpret your answer to  
20      Staff's Data Request 3.17 to mean that the Company  
21      will not prepare a cost of service study for CUCI on a  
22      stand-alone basis as part of the process in

1 determining whether or not there are demonstrated  
2 savings?

3 A. Could I have that read back, please?

4 (Whereupon the requested portion  
5 was then read back by the  
6 Reporter.)

7 A. You are correct. We will not prepare a  
8 cost of service study for the entire Citizens  
9 stand-alone company, if that is the question.

10 Q. Well, okay. I am just trying to  
11 understand what you intend to do in trying to  
12 reconcile what I think was an answer given to me by  
13 Mr. Gloriod and your answer to IIWC Data Request 2-2  
14 and now Staff Data Request 3.17. Because I was under  
15 the impression that as part of the SSP you would  
16 prepare, and I just said, a cost of service study for  
17 CUCI on a stand-alone basis and use that as a measure  
18 in determining whether or not there was demonstrated  
19 savings. And your answer to Staff's data request  
20 seems to suggest to me that it won't be a full-blown  
21 cost of service study. Am I reading that correctly?

22 A. That's right.

1           Q. What kind of cost of service study do you  
2 intend to prepare for CUCI on a stand-alone basis?

3           A. It would make the terminology  
4 stand-alone. When we are discussing stand-alone, I am  
5 referring to stand-alone pre-acquisition. I believe  
6 Mr. Gloriod was referring to the CUCI rate area as  
7 opposed to the proposed acquisition. We would have a  
8 cost of service study for the Citizens' rate areas, if  
9 they are in for a rate case. And to that extent those  
10 rate areas will be identified separately from other  
11 rate areas or service areas.

12                 So if the reference to stand-alone deals  
13 with post-acquisition rate of service areas, then,  
14 yes, we would prepare a cost of service study. If you  
15 are referring to a stand-alone on a pre-acquisition  
16 basis, no, we would not prepare a full cost of service  
17 study for the entire Citizens' cost of service on a  
18 stand-alone pre-acquisition basis.

19           Q. Let me see if I understand your answer,  
20 okay. Assuming the acquisition takes place, assume  
21 within the year a rate case was filed on behalf of  
22 CUCI, and in conjunction with that rate case there

1 will be a cost of service study for CUCI. Are you  
2 with me?

3 A. Yes.

4 Q. And there is the SSP is in place and some  
5 amount of savings go to ratepayers and some amount of  
6 savings go to pay off the acquisition premium. Three  
7 years later another rate case is filed, okay. What  
8 kind of -- you will have a cost of service study for  
9 CUCI and IAWC on a combined basis at that point,  
10 correct?

11 A. We will if those particular rate areas  
12 are in for a rate increase at that time, yes. We will  
13 be measuring cost of service. We are using the term  
14 cost of service study. There could be cases where the  
15 Company doesn't automatically file a cost of service  
16 study, but we would be measuring cost of service for  
17 each individual rate area that would be in for a rate  
18 case at that time.

19 Q. All right. Well, let's assume that it's  
20 a rate case three years afterwards that's not on a  
21 combined basis, so it's a new CUCI rate case and you  
22 have a cost of service study for that rate case. At

1       that point how would you then look to determine  
2       whether or not there were demonstrated savings  
3       vis-a-vis, I guess, that cost of service study?

4               A. Well, the demonstrated savings would  
5       result from identifying each savings event resulting  
6       from the acquisition. In most cases those savings  
7       events will be captured after integration of the two  
8       companies. Some other savings events such as capital  
9       expenditure savings, material cost savings to capital  
10      expenditures will continue to evolve and grow  
11      exponentially. We would be identifying the foregone  
12      costs within the cost of service and that's what we  
13      would be measuring. And that would be measured  
14      through identifying each individual savings event and  
15      measuring the savings that are in, say, year three in  
16      your example.

17             Q. Let me follow up on that. Again in this  
18      hypothetical, within the year you file a new rate  
19      case, you have a new cost of service study. Three  
20      years later, that's where we are at, okay, and you are  
21      going to file a cost of service study for CUCI. All  
22      along you will have in a separate bucket these

1       demonstrated savings you will be tracking, these  
2       savings events that you call them, and that will be a  
3       number. So you file your rate case and you have got  
4       your cost of service study and then you are going to  
5       assume that the reason why your cost of service study  
6       is where it's at is in part because you have been able  
7       to accumulate these savings over here in this bucket,  
8       right?

9               A. Correct.

10              Q. Now, in order to prove that the cost of  
11       service study is filed and is as low as it is because  
12       of this bucket of savings, you have to have or do you  
13       intend to have a sort of a hypothetical cost of  
14       service study so that you can say if we hadn't had the  
15       acquisition and our cost of service study would have  
16       been X plus, by taking away the demonstrated savings  
17       now we are back down to the cost of service study as  
18       filed. So you have to have sort of this hypothetical  
19       cost of service study, do you not?

20              A. I don't believe you would, no.

21              Q. You don't intend to do that?

22              A. Not as I understand it from your

1 question, no. If I understand correctly, you are  
2 referring to measuring the entire Citizens on a  
3 stand-alone basis pre-acquisition, every cost, every  
4 cost of service component. That's my understanding of  
5 your inquiry.

6 Q. I really want to understand what you plan  
7 to do. My questions aside, as inarticulate as they  
8 may be, I am just trying to understand what you are  
9 going to do at the point of time you file a cost of  
10 service study. All along you have got this bucket of  
11 demonstrated savings. My point is that this cost of  
12 service is as low as it is because you have been able  
13 to accumulate these savings. We are together right  
14 there?

15 A. Correct.

16 Q. And now you have got to prove that those  
17 demonstrated savings did in fact put the cost of  
18 service study where it is when you filed it, right?

19 A. Correct.

20 Q. And how are you going to do that?

21 A. Well, I believe I have explained that in  
22 my testimony. We would identify each savings event,

1       and I am going to refer back to page 2 of my  
2       surrebuttal. What I have indicated in surrebuttal  
3       testimony is that -- and this is premised on  
4       identifying and tracking each individual savings event  
5       that would occur. And by savings event I am referring  
6       to, for example, each individual position that's  
7       eliminated. And that's an example of a savings event.

8                       I have said detailed information will be  
9       maintained for the specific savings event associated  
10      with, in this case, the elimination of a billing clerk  
11      position. And I go on to explain that we will keep  
12      detailed information about what that position function  
13      was, the fact that that position was eliminated as a  
14      direct result of the acquisition, and by  
15      demonstrating, for example, that the elimination of  
16      that position was a direct result of the acquisition,  
17      and then measuring that savings.

18                     That will be substantially the method we  
19      will use to show that. I go on to explain that  
20      further in testimony and can read that if we need to.

21                     Q. Let me ask it one more way. Then I will  
22      move on perhaps, okay. Staying with, again, with my

1 sort of vulgar description of your SSP and the second  
2 rate case three years after the first case and you  
3 have got this cost of service study filed and you have  
4 got this bucket of demonstrated savings, your point  
5 would be that if I prove and justify that demonstrated  
6 bucket of savings, I will have in effect proven that  
7 the cost of service study would have been otherwise  
8 higher by that same amount?

9 A. Yes, that's technically correct. I  
10 wouldn't characterize it as a bucket of savings. We  
11 would be identifying each individual savings event,  
12 showing that the savings were a direct result of the  
13 acquisition, and showing that savings still exist,  
14 say, in year three, and that in year three those same  
15 savings would still exist that there wouldn't have  
16 been exogenous factors, for example, that would have  
17 caused those savings to no longer exist. By  
18 demonstrating that those savings still exist, they are  
19 directly tied to the acquisition. That also is  
20 indicative that, absent the acquisition, those savings  
21 would not have been there, and as a result they would  
22 be in the stand-alone cost of service.

1           Q. Do me a favor. Go back to our IIWC Data  
2 Request Number 2-2. Again, it was mine.

3           A. I have that.

4           Q. I will just sort of summarize again this  
5 answer that we have been talking about. Acquisition  
6 savings will be determined in future rate proceedings  
7 by comparing the then test year operational costs to  
8 the costs that would have existed had the Company  
9 remained a stand-alone utility. So given your prior  
10 answers then, when you talk about operational costs,  
11 the bulk of the demonstrated savings are intended to  
12 be employee related, employee reduction, correct?

13          A. That's one significant area, yes.

14          Q. And so you will look at -- well, that  
15 will be the operating -- in my question back to you,  
16 those are the costs that you would be looking at on a  
17 stand-alone basis in order to arrive at your  
18 determination that there have been demonstrated  
19 savings?

20          A. Yes. In this answer I am referring to  
21 the operating costs necessary to measure the costs  
22 that have been eliminated and are being identified as

1 a savings event.

2 Q. You are not talking about all operational  
3 costs that make up or are part of the cost of service  
4 study. You are talking about the operational costs  
5 that are shown on your exhibit attached to your direct  
6 testimony, the 15, 16 categories of costs?

7 A. Essentially, yes. I am talking about any  
8 operating costs that would be necessary to evaluate to  
9 determine whether the savings events still exist and  
10 whether the savings are the direct result of the  
11 acquisition.

12 Q. Now, I know that in the record we are  
13 looking at 25 positions that will be reduced, but in  
14 fact it was 30 positions that would be reduced but  
15 five positions that were a result from the  
16 acquisition, correct?

17 A. Correct.

18 Q. Does the Company plan to track the costs  
19 and expenses associated with the increased costs  
20 associated with the acquisition?

21 A. Yes. Savings events can technically go  
22 either direction. They could be positive or negative

1 savings. In this case the five additional positions  
2 would be tracked just like the elimination of 30  
3 positions and continually measured for how those costs  
4 go up over time. They would then be netted against  
5 other labor savings to derive at the end result, the  
6 acquisition savings.

7 Q. So you do intend to track increased costs  
8 associated with the acquisition?

9 A. Yes, we intend to track increased costs  
10 that are a result of the acquisition. If we have what  
11 I would term to be a negative Synergy, we would track  
12 that.

13 Q. So, I mean, you may not know right now  
14 today that as a result of the acquisition you are  
15 going to have a particular cost that's only because of  
16 the acquisition, correct?

17 A. Correct.

18 Q. And so does that mean that every cost --  
19 you know lawyers like to deal in extremes -- every  
20 cost that the Company incurs it's going to have to  
21 look at and say, well, that's a cost because of the  
22 merger only or, not the merger, the acquisition, or

1       it's not a cost because of the acquisition, or that's  
2       a savings because of the acquisition, or it's a  
3       savings irrespective of the acquisition? Are you  
4       going to have to look at every cost in that way?

5               A. No, I don't believe it's necessary to  
6       look at every cost that way. There will be actions  
7       that will lead us to identify whether the cost is  
8       related to the acquisition. For example, in most  
9       cases if we have additional costs that's a direct  
10      result of the acquisition, that's what's identified at  
11      the time of the integration process. And, in fact,  
12      items have already been identified by the integration  
13      team, and I have incorporated that into my savings  
14      analysis here.

15              I don't automatically have a reason to  
16      believe that we would have costs going up because of  
17      the acquisition in and of itself, other than what I  
18      have identified so far in the model that the  
19      integration team have identified. And those typically  
20      would occur at the time of the acquisition, as would  
21      most of the cost savings.

22              Q. For the five positions that are the

1 result of the acquisition, have you assumed the same  
2 level of wages and the same level of employee benefits  
3 in your modeling and in your exhibits that are  
4 attached to your testimonies?

5 A. Same level as what?

6 Q. I'm sorry, as the positions that are  
7 being eliminated because of the acquisition?

8 A. No. The salaries that are in here for  
9 those five positions are our best estimate at this  
10 time as to what the actual salaries will be for those  
11 five positions when they were added after the  
12 integration.

13 Q. I guess the better question would have  
14 been, Mr. Stafford, where in your exhibits could I  
15 find the expected acquisition cost increase by virtue  
16 of these five positions?

17 A. Essentially, in my workpapers there is  
18 some workpapers that were provided in response to one  
19 of the IIWC data requests and one of the more specific  
20 papers that I provided in response to an MHE data  
21 request that identifies those. But they are also  
22 listed within some workpapers I provided in response

1 to one of your data requests. In sum total there is a  
2 listing of five positions being added, an estimated  
3 increase in salary from that, and then adjustments,  
4 negative savings, were reflected for any labor-related  
5 category such as group insurance, pensions.

6 Q. Going back to your Exhibit 3.5 attached  
7 to your rebuttal testimony, under Column 1, the  
8 Synergy Savings?

9 A. Yes.

10 Q. Is that net Synergy savings? Does that  
11 take into account the five positions that are created  
12 as a result of the acquisition?

13 A. Yes, it does.

14 Q. And there are workpapers that support  
15 that, you said?

16 A. Yes, the workpapers provided to IIWC were  
17 on an electronic spreadsheet. I believe they were in  
18 response to 3-1. They were provided in electronic  
19 format.

20 Q. And the Company would track these  
21 acquisition costs, the increased acquisition costs,  
22 over the 40-year amortization period as well?

1           A. I am not sure what you mean by increased  
2 acquisition costs.

3           Q. Well, the costs that occur only because  
4 of the acquisition, not the savings, but costs like  
5 the five positions that we have been talking about,  
6 you will track those costs over four years, would you  
7 not?

8           A. That is correct.

9           Q. And all other costs would occur only  
10 because of the acquisition?

11          A. Correct, within reason. I mean, if there  
12 is a cost deemed immaterial, or savings or a cost,  
13 either one, and I am saying that would be a thousand  
14 dollars, we may not track that. I do have one cost in  
15 here that's \$10,000 in my model. So within reason we  
16 will do that.

17          Q. Are you familiar with the -- we are going  
18 to really move to something different now. Are you  
19 familiar with the infrastructure maintenance charge in  
20 the rulemaking?

21          A. Yes.

22          Q. And you know the purpose and rationale

1       behind the infrastructure maintenance charge?

2               A.   Yes.

3               Q.   Is it anticipated that the Shared Savings  
4       Plan as proposed by the Company would involve in any  
5       way or have any relationship to the infrastructure  
6       maintenance charge if ever one was approved for IAWC?

7               A.   I don't believe it would, no. To the  
8       extent that it would, certainly, then adjustments  
9       would be made within the Synergy model. Right now I  
10      cannot anticipate a reason why it would.

11              Q.   Talk a little about the purported  
12      savings, and I believe it is expected that there would  
13      be some savings in the area of regulatory expenses?

14              A.   Correct.

15              Q.   Now, am I correct in understanding that  
16      today CUCI presently does not have any regulatory  
17      staff? Well, at least regulatory staff dedicated  
18      solely to the functions that have been performed by  
19      this business discipline?

20              A.   That's correct.

21              Q.   And that to the extent that CUCI needed  
22      any kind of regulatory assistance, it had received

1       that from its parent company?

2               A.   Correct.

3               Q.   Exhibit 3.1.

4               A.   Yeah.

5               Q.   Exhibit 3.1 where you outline the  
6       acquisition savings under Column 7, the Regulatory  
7       Expense, is that the level of the regulatory expense  
8       that was shown or reflected in CUCI's rates back in  
9       1994?

10              A.   No, it is not.

11              Q.   It's not?

12              A.   No, because I anticipated that not all  
13       the regulatory expense would be eliminated. I  
14       estimated that 20 percent of the annual amortization  
15       level of regulatory expense would be needed by  
16       Illinois-American on a post-acquisition basis or in  
17       other words that regulatory expense would actually  
18       increase by a portion of the amount that CUCI agrees  
19       they had.

20              Q.   That portion of the ratio, though, was  
21       developed looking at the regulatory expense level out  
22       board rates in the 1994 case?

1           A.   Correct.

2           Q.   Let me ask you to turn to page 4 of your  
3   rebuttal testimony.  There on lines 16 and then onward  
4   you address the question about the 12 percent  
5   corporate overhead charge on construction projects  
6   that could be eliminated without the acquisition, or  
7   Mr. Gorman's contention that that would be the case.  
8   Am I correct in understanding in your response to IIWC  
9   Data Request 2-1(b) that your position is in part that  
10   because of American Water Work's ownership, the  
11   operational costs are retained at the parent company  
12   level and not billed to operating subsidiaries?

13          A.   Correct.

14          Q.   So if CUCI had been just one of the 22 or  
15   23 operating subsidiaries of American Water Works, it  
16   would have been the beneficiary of the AWW being able  
17   to provide this service without any costs being  
18   attributable to this service?

19          A.   I believe a clarification is needed  
20   before I fully answer that.  When I am referring to  
21   American Water Works' operational costs, I am  
22   referring to the parent company itself, American Water

1 Works' parent. None of these operational costs go  
2 down to the subsidiary.

3 Costs for American Water Works Service  
4 Company do go down to the subsidiary to the extent  
5 that they work directly on a capital project and they  
6 charge direct time to those projects. But they do not  
7 through their billing system automatically charge in  
8 this case, in the case of Citizens, 12 percent of  
9 their costs, service company costs, to capital  
10 projects and the other 88 percent to operating costs.

11 American Water Works Service Company  
12 direct bills its time out, time directly to projects.  
13 The 12 percent is a portion of the Stanford costs and  
14 public service organization costs that go directly to  
15 the capital projects, the other 88 percent to  
16 operating costs. It's a different type of billing  
17 system than what American Water Works Service Company  
18 has. The end result is that a hundred percent of  
19 those costs, service company type costs, are billed  
20 out. They are just billed out differently.

21 Q. Thank you. Let me ask you to turn to  
22 page 5 of your rebuttal testimony, the question that

1 starts on line 14 and the answer that begins on line  
2 18. There you respond to Mr. Gorman's claim that the  
3 savings attributable to lowering CUCI's common equity  
4 ratio and reducing its overall cost of capital should  
5 not be attributable to the cost of acquisition. And  
6 again in reviewing your answer, Mr. Stafford, it  
7 appears that since 1984 that CUCI's common equity  
8 ratio has been declining. Would that be a fair  
9 statement?

10 A. Correct.

11 Q. And that the common equity ratio of 65  
12 percent in 1984 and 1985 was at a time of high  
13 inflationary periods?

14 A. Yes, I would agree with that. I don't  
15 know if that's the reason why the ratio was higher,  
16 but I agree with that comment.

17 Q. Do you have any knowledge now as to what  
18 CUCI common debt ratio would be if it were to file a  
19 rate case today?

20 A. If they were to file a rate case today,  
21 the ratio, I know, would be -- the common equity  
22 ratio -- would be lower, and that's in large part due

1 to the decision by Citizens to go strictly into the  
2 telecommunications area. They have purchased a number  
3 of telecommunications properties, incurred a lot of  
4 additional debt, and to date I am not aware of them  
5 having received funds from any of their proposed sales  
6 of water, wastewater, gas and electric property. So  
7 the ratio would be higher when it is considered to be  
8 representative of Citizens on a long term basis.

9 Q. Let me ask you to turn to your  
10 surrebuttal testimony. There is some light at the end  
11 of this tunnel. You talk about the, going back to an  
12 earlier subject, talk about tracking of the  
13 demonstrated savings and the things that the Company  
14 will do. And you indicate that the information that  
15 will be accumulated will include a summary of the  
16 specific functions performed by the positions on a  
17 pre-acquisition basis, is that right?

18 A. Correct.

19 Q. I guess the question is, I mean, assuming  
20 the acquisition takes place, IAWC then will attempt to  
21 discern what are the specific functions of these  
22 different positions or do you know that information

1       today?

2               A. Well, it's a fairly easy matter for us to  
3       get that information. We can obtain that directly  
4       from Citizens. And although I wasn't directly  
5       involved in the process, I believe Mr. Gloriod was  
6       involved in discerning what those functions were and  
7       whether those functions were duplicative of other  
8       functions that are performed.

9               Q. You know, the testimony here says on a  
10       pre-acquisition basis. How would you know what the  
11       CUCI employees' functions were if you are not -- if  
12       you don't own the company, you can't be there in their  
13       offices figuring this stuff out, can you? They going  
14       to let you in?

15              A. Well, it's part of the integration review  
16       process. You do have access to the records of CUCI  
17       and you can get payroll-related information to assess  
18       in part. In fact, you can trace it back even further  
19       with due diligence. But you need to make an  
20       assessment of what your potential savings are from the  
21       acquisition, even at an early stage. So you do have  
22       access to payroll information and you can make it --

1     you have special information to determine what those  
2     functions are. Because without that information, you  
3     can't assess whether you need that function after the  
4     acquisition.

5             Q. Does IAWC have access to this  
6     pre-acquisition function information as of today?

7             A. I believe it does. I believe it would  
8     have. I may not be the best witness to answer that.  
9     As I say, the information was reviewed during the  
10    process of integration and there was sufficient  
11    information to determine what the general functions of  
12    that position were.

13            Q. So you are telling us that your review of  
14    the pre-acquisition functions related to these  
15    different positions is in progress and that more  
16    information will have to be accumulated, is that a  
17    fair statement?

18            A. Well, I think that process as a whole is  
19    a dynamic process. You know, as I set here today I  
20    have provided information on estimated labor savings.  
21    You know, the process of identifying what those exact  
22    labor savings are is dependent in large part on what

1 positions are eliminated. So I would say that's a  
2 process that is not complete as of today. As  
3 Mr. Gloriod testified, he commented that we have  
4 identified three union positions for elimination but  
5 did not automatically say that there may not be other  
6 reductions. So it is somewhat a dynamic process.

7 Q. Right. There is a difference between  
8 having decided that you are going to eliminate a  
9 position and your obligation under your own plan to  
10 prove in a future rate case that these are the  
11 functions of that reduced or eliminated position which  
12 could not have been affected by these other factors,  
13 outside factors, or anything of that sort. And the  
14 question really is, have you captured today all of the  
15 information that you need to know, as you described  
16 it, the pre-acquisition functions, do you have all  
17 that information today?

18 A. Do I personally have that?

19 Q. No, does the Company have it, somebody in  
20 the Company have this information?

21 A. I believe some one does. I don't know for  
22 sure whether that's the case.

1           Q. And then on page 3 of your testimony  
2       where you are sort of describing this process, you  
3       know, you talk in terms of a billing clerk position  
4       being eliminated and you indicate that the Company  
5       would look at these different factors, including  
6       technology, to see whether or not that would have a  
7       bearing on whether or not the demonstrated savings  
8       associated with that billing clerk's position having  
9       been eliminated would continue or not, correct?

10           A. Correct.

11           Q. When you look at, for example, a factor  
12       such as improved technology, would one of the  
13       considerations be whether or not that technology was  
14       also available to CUCI?

15           A. Certainly.

16           Q. I will just check my notes real quick.  
17       Would you turn to page 7 of your direct testimony?

18           A. I have that.

19           Q. There on lines 12 through 22 you refer to  
20       an alternative ratemaking proposal that's also  
21       discussed by Mr. Ruckman, correct?

22           A. Correct.

1           Q. Is this an alternative ratemaking  
2     proposal that would be made pursuant to Section 9-244  
3     of the Public Utilities Act?

4           A. Would you refresh my memory on 9-244?

5           Q. It's the section under Article 9 that  
6     sets out the ratemaking authority for the Illinois  
7     Commerce Commission that gives the Commission  
8     permission to authorize alternative ratemaking.

9           A. I don't believe that this proposal was  
10    made in the context of 9-244. The proposal was made  
11    for consideration by the Commission as an alternative  
12    to the Company's primary proposal in the context of  
13    this proceeding. I don't believe it was filed under  
14    9-244.

15          Q. Was it intended to be an alternative  
16    proposal under Section 7-204?

17          A. Yes.

18          MR. FITZHENRY: Thank you, Mr. Stafford.  
19    That's all the questions I have.

20          EXAMINER SHOWTIS: I have a few questions.

21

22

1 EXAMINATION

2 BY EXAMINER SHOWTIS:

3 Q. Which proposal do you believe is more  
4 favorable in terms of ratepayer interests, the SSP or  
5 the alternative ratemaking proposal? And then if you  
6 believe that one is more favorable than the other, I  
7 would like for you to explain why.

8 A. If you are referring to more favorable to  
9 ratepayers being which one provides the most savings  
10 in terms of dollar savings to ratepayers, the SSP as  
11 proposed by the Company provides that the ratepayers  
12 will get the first ten percent of any savings. I  
13 believe under the alternative ratemaking proposal that  
14 the -- in both proposals there are demonstrated  
15 savings required because of the adverse impact  
16 provision of 7-204.

17 Under the alternative ratemaking proposal  
18 I believe that a hundred percent of the demonstrated  
19 savings would go to cover the acquisition revenue  
20 requirement indirectly, while under the SSP only 90  
21 percent of the savings would go to cover the  
22 acquisition revenue requirement. Therefore, in terms

1 of which one would the ratepayers benefit more  
2 monetarily, they would benefit more from the SSP.

3 Q. On page 4 of your direct testimony and  
4 also continuing on to page 5, you describe the SSP in  
5 the manner that was described by Mr. Ruckman?

6 A. Correct.

7 Q. Is it correct that the SSP is basically  
8 addressing two factors or two matters. One is the  
9 acquisition adjustment which is accounted for through  
10 the acquisition revenue requirement, and then the  
11 second main factor in the SSP is the demonstrated  
12 savings which are allocated between shareholders and  
13 ratepayers in the manner set forth therein, is that  
14 correct?

15 A. Correct.

16 Q. So there is basically two factors we are  
17 dealing with?

18 A. Yes.

19 Q. Various witnesses that have been  
20 presented on behalf of IAWC have emphasized the  
21 benefits associated with the SSP and they have placed  
22 particular emphasis on, some have called it, the no

1 net cost standard or no adverse rate impact on  
2 ratepayers from the SSP, is that correct?

3 A. Correct.

4 Q. Now, if you would turn to Exhibit 3.5R  
5 which is part of your rebuttal presentation.

6 A. I have that.

7 Q. Let's assume for purpose of this question  
8 that the savings shown there are actually  
9 demonstrated. I realize there is some estimated  
10 figures, but let's just assume that these are the  
11 actual figures.

12 A. Okay.

13 Q. I am assuming for purposes of these  
14 questions that I am a ratepayer in the CUCI service  
15 territory, and I believe you indicated or there has  
16 been testimony that 95 percent of the demonstrated  
17 savings would be more or less attributable to the  
18 former CUCI service territory, is that correct?

19 A. Correct.

20 Q. So I am a ratepayer and I am looking at  
21 Exhibit 3.5R and I see two columns that I am  
22 interested in. One is the recoverable premium revenue

1 requirement over the 40-year period, and I would  
2 assume as a ratepayer that recoverable means that  
3 those moneys would flow through to the shareholders.  
4 And then as a ratepayer I would also look at Column A  
5 and I would say, well, that looks pretty good. That  
6 is accumulative rate savings for customers that I  
7 would be sharing at.

8                   So then I go down to the bottom of that  
9 exhibit and I think well maybe net present value might  
10 be a good way of looking at things, rather than  
11 accumulative figures. And as a ratepayer I look and I  
12 say, wait a minute, the net present value of the  
13 recoverable premium revenue requirement that's going  
14 to shareholders is \$55.8 million. So I am thinking,  
15 well, accumulative rate savings for me are going to  
16 have to be better than that if I am going to be better  
17 off. I go to Column 8 and I say, holy smokes, the  
18 accumulative rate savings for me is \$16 million.

19                   And so it appears that the accumulative  
20 or that the recoverable premium revenue requirement on  
21 a net present value basis is about three and a half  
22 times the accumulative rate savings for customers.

1 And as a customer I then ask how am I better off; this  
2 looks like I am worse off with this proposal. Would  
3 you answer my concerns?

4 A. Sure, I would be glad to. Column 8  
5 represents 16 million net present value of savings  
6 that you as a customer or ratepayer would not have  
7 absent the acquisition. And that 16 million of  
8 savings comes as a result, and only the result, of the  
9 acquisition and came to you at no risk on your part,  
10 and in fact the documents and testimony have a number  
11 of reasons, particularly the testimony of Mr.  
12 Kelleher, where you are not only getting \$16 million  
13 of present value quantifiable benefits, but you are  
14 getting a substantial level of qualitative benefits  
15 also. So 16 million is coming to you at no cost, at  
16 no risk on your part, with additional benefits on top  
17 of the 16 million in the form of qualitative benefits.

18 What's going to the shareholders is  
19 almost a full recovery but not quite a full recovery  
20 of its investment it made in providing these savings.  
21 In Column 3, the net present value revenue requirement  
22 is the investment that shareholders made to attain

1       these savings of \$75 million. And what the  
2       shareholders are getting back out of that is 55  
3       million of net present value savings in Column 5 plus  
4       50 percent of the excess savings in Column 6. Also I  
5       might add that the other 50 percent of the savings in  
6       Column 6 is going to ratepayers. The ratepayers are  
7       actually getting over 24 million of net present value  
8       savings.

9                       So the end result is that the  
10       shareholders have taken the entire risk of providing  
11       savings and they have not fully recouped their entire  
12       investment of 76 million net present value. They are  
13       actually still slightly in the hole. And ratepayers  
14       for no risk have gotten in excess of 24 million in  
15       savings plus substantial qualitative benefits from the  
16       acquisition. So this schedule demonstrates that  
17       ratepayers have faired better than shareholders under  
18       our proposal.

19                    Q. I realize in looking at Exhibit 3.5R that  
20       there is a portion of the -- well, here you use  
21       premium -- but acquisition adjustment that is not  
22       recovered through the revenue requirement?

1           A. That's correct, over 19 million is not  
2 recovered.

3           Q. So 19 million is not recovered. But it  
4 still appears to me that ratepayers -- on a net  
5 present value basis over the 40-year period ratepayers  
6 are paying through rates \$55.8 million which would  
7 allow recovery of a significant percentage of the  
8 acquisition premium. And for that \$55.8 million on a  
9 net present value basis they are getting 16 million of  
10 savings.

11          A. The 55 million that you are referring to  
12 is not going to increase rates to customers. They are  
13 not paying any more in their rates than they would  
14 have prior to the acquisition. That's a commitment  
15 that the Company made, to have no adverse rate impact  
16 on the customers whatsoever.

17                 What the 55 million represents is a  
18 recovery of the portion of the demonstrated savings, a  
19 portion of the savings that have gone to already  
20 reduce cost of service, and have gone to lower, for  
21 lack of a better term, the amount that the customers  
22 have paid through rates as a direct result of the

1 acquisition. So customers are not paying any more.  
2 They are paying less under our proposal. And the 55  
3 million is only being recovered by the Company because  
4 it represents demonstrated savings that have gone to  
5 otherwise reduce customer rates.

6 Q. Well, Column 5, the Recoverable Premium  
7 Revenue Requirement, just so I am clear, on a net  
8 present value basis, that \$55.8 million, is that total  
9 on the net present value basis the amount that would  
10 be reflected in rates?

11 A. That's the amount that would be reflected  
12 in rates and it is only recovered from savings that  
13 are also reflected in rates. It's not coming from  
14 additional rates to customers. It's coming only from  
15 savings that have gone to lower the cost of service  
16 prior to that adjustment.

17 Q. What about Column 8? Is that net present  
18 value amount, roughly 16.1 million, is that reflected  
19 in cost of service or rates for ratemaking purposes?

20 A. Yes. Column 8 savings of 16.1 million,  
21 along with 50 percent, essentially the dollar amount  
22 shown in Column 6 as additional savings that are

1 reflected in rates, and have gone to lower the cost of  
2 service that ratepayers have to pay.

3 Q. Why do you say along with Column 6?

4 Because it appears to me that if you add Column 6 to  
5 Column 7, you get Column 8. Column 6 won't be in  
6 addition to Column 7, would it?

7 A. I'm sorry. I stand corrected. You are  
8 correct. Column 6 is included in the total in Column  
9 8. So we are talking about 16.1 million in total.

10 Q. If I understand what you are saying,  
11 Column 8 is reflected in rates. But Column 5 is not  
12 necessarily reflected in rates?

13 A. Correct. And Column 8 is reflected in  
14 rates as savings to customers, lower cost of service.

15 Q. Just one last question then with regard  
16 to Column 5. What then does Column 5 exactly  
17 represent? Because it's titled "Recoverable Premium  
18 Revenue Requirement." Is that the amount of the  
19 premium that would be recovered by shareholders?

20 A. That's correct. That is the amount of  
21 premium that would be recovered by shareholders, the  
22 investment that they made, and acquiring any assets of

1 Citizens. And it's recovered entirely from  
2 demonstrated savings resulting in no increase in cost  
3 of service to customers.

4 Q. Just one last question then with regard  
5 to the amount in Column Number 5. From whom are those  
6 amounts then being recovered?

7 A. Those amounts are being recovered from  
8 the savings themselves that have resulted from the  
9 acquisition.

10 Q. Well, is any of the amount shown in  
11 Column 5 being recovered from ratepayers?

12 A. If by ratepayers you mean through  
13 increased rates, the answer is no.

14 EXAMINER SHOWTIS: That's all I have.

15 MR. SPRINGER: Mr. Examiner, I would request  
16 a brief recess at this time.

17 EXAMINER SHOWTIS: Okay.

18 (Whereupon the hearing was in  
19 a short recess.)

20 EXAMINER SHOWTIS: Let's go back on the  
21 record for redirect.

22 MR. SPRINGER: We do have some brief

1       redirect, Mr. Examiner.

2                               REDIRECT EXAMINATION

3                       BY MR. SPRINGER:

4                       Q.   Mr. Stafford, during questioning you were  
5       asked about inclusion in the Company's current rate  
6       case of certain costs which were disallowed in the  
7       Northern Illinois Water Corporation/Illinois-American  
8       Order, Docket 99-0418.  Would you care to clarify your  
9       response to that question?

10                      A.   Yes, I would be glad to.  The costs in  
11       question are still subject to appeal on the part of  
12       the Company.  They are costs that the Company  
13       certainly believes are legitimate recoverable costs,  
14       subject to appeal.  We requested that they be included  
15       in the revenue requirement in the proceeding.  Staff  
16       proposed to make an adjustment to remove those costs,  
17       and the Company accepted for purposes of that case  
18       that adjustment.  We did not on rebuttal testimony ask  
19       that we would continue to recover those in that  
20       proceeding.  We do, however, reserve the right if we  
21       win the appeal to ask for recovery of those costs in a  
22       future proceeding.

1           Q. You were also asked a question with  
2   regard to whether customers vote for directors of the  
3   Company. Do you have a clarification of your answer  
4   to that question?

5           A. I did misspeak in responding to that  
6   question. Directors of the Company are voted on in  
7   part by customers because there are customers that are  
8   shareholders of the Company and they do have a vote in  
9   who are elected to the board of directors of the  
10   Company.

11          Q. And which shareholders would you be  
12   referring to there, Mr. Stafford?

13          A. I am referring to preferred stockholders  
14   of the Company.

15          Q. You also, I believe, in response to a  
16   question indicated that there were certain  
17   disallowances of expenses in both the Northern  
18   Illinois Water Corporation/Illinois-American Order,  
19   Docket 99-0418, and also in the  
20   Illinois-American/United Water Order, Docket 99-0457.  
21   Do you have a clarification to your response to that  
22   question?

1           A. Yes, I do. The Company entered into a  
2 stipulation under which the Company would not agree to  
3 request recovery of any cost associated with the  
4 acquisition in United Water. As a result of that  
5 stipulation, there were technically no disallowed  
6 costs in that proceeding.

7           Q. Turning now, Mr. Stafford, to your  
8 Exhibit 3.5R which was the subject of some  
9 questioning.

10          A. I have that.

11          Q. You were asked, I believe, by the Hearing  
12 Examiner about a comparison between the net present  
13 value savings realized by customers as shown in Column  
14 8 and the net present value of the recoverable portion  
15 of the acquisition premium as shown in Column 5.  
16 Would you comment on that comparison?

17          A. Yes, I would be glad to. In order to  
18 bring about the savings in this acquisition, the  
19 Company has effectively incurred costs that are  
20 reflected in Column 3, \$75.7 million of costs.  
21 Through the Company's sharing proposal it is proposing  
22 to recover on a present value basis, under the

1       assumption that forecasted savings equal actual  
2       savings and so forth, that recovery of 55.8 million in  
3       Column 5, and 50 percent of any excess savings  
4       represented by the numbers in Column 6.

5                     In summary, the investment that the  
6       shareholders place in the acquisition, the recovery of  
7       that investment, is only 55.8 million, what's  
8       reflected in Column 5, plus the 8 million in Column 6.  
9       The net result is that the Company is investing almost  
10      76 million and is recovering approximately 56 million  
11      plus 8 million, resulting in a shortfall of 12  
12      million. That's the net result to shareholders from  
13      this acquisition, is that on a net present value basis  
14      shareholders would recover negative 12 million in  
15      their investment and ratepayers would get a positive  
16      16 million reflected by the savings in Column 8.

17                    Q. So the negative 12 million you refer to  
18      is the number which should be compared to the positive  
19      approximately 16.1 million realized by ratepayers, is  
20      that correct?

21                    A. That's correct.

22                    Q. And that negative \$12 million is the net

1 present value effect upon the shareholder of the  
2 proposal, is that correct?

3 A. That's correct.

4 Q. You were also asked some questions about  
5 reasons why from the customer perspective the Savings  
6 Sharing Proposal is a favorable proposal, is that  
7 correct?

8 A. Yes.

9 Q. Do you have an illustration which you  
10 believe will indicate that point?

11 A. Yes, I do.

12 Q. Would you give that, please?

13 A. Trying to do it from a ratepayer's  
14 perspective, but prior to the acquisition a Citizens'  
15 customer on average, I am guessing, has about a \$30  
16 water bill. It could be higher; it could be lower.  
17 So that's their water bill today. As a result of the  
18 acquisition, for illustrative purposes, I am going to  
19 say that savings are identified from the acquisition  
20 of \$10, the equivalent of \$10, on that water bill. Of  
21 that \$10 savings, the first ten percent of this  
22 savings or \$1 will go first to the ratepayers and the

1 remaining \$9 will cover a portion of the investment, a  
2 portion of or all of the annual revenue requirement  
3 associated with making the investment that generated  
4 the savings. So the end result is that a customer  
5 prior to the acquisition would have a \$30 water bill.  
6 After the acquisition they would have a \$29 water  
7 bill. And thus ratepayers as a result would see \$1 of  
8 savings. The remaining \$9 of savings would go to  
9 cover a portion of the investment that the Company  
10 made to generate those savings.

11 Q. Mr. Stafford, under the Savings Sharing  
12 Proposal in your hypothetical is there any risk  
13 associated -- excuse me, any risk upon the ratepayer  
14 with regard to whether there will be realization of  
15 the savings?

16 A. No, there is not. Under the Company's  
17 proposal ratepayers would never, ever in any event see  
18 a larger water bill as a result of the acquisition  
19 than they would have had absent the acquisition. So  
20 if the Company never had to raise rates for any other  
21 reason, all other things being equal, over a 40-year  
22 period the \$30 water bill would stay intact. The

1 worse the customer would ever do would have a \$29  
2 water bill with the acquisition. If the Company could  
3 not prove that the other \$9 of savings existed and  
4 were the result of the acquisition, then the customers  
5 would have in that case even a lower water bill. The  
6 shareholders would be eating even more of the  
7 investment. But the worse they would ever do is have  
8 a water bill \$1 lower than what they would have had  
9 absent the acquisition.

10 Q. That assumes that the \$1 portion,  
11 ratepayer portion, of savings had been demonstrated,  
12 is that right?

13 A. That's correct.

14 MR. SPRINGER: Thank you. That's all the  
15 questions we have for Mr. Stafford at this time.

16 RE CROSS EXAMINATION

17 BY MS. VON QUALEN:

18 Q. Is it your testimony, Mr. Stafford, that  
19 the disallowed costs in 99-0418 were intentionally  
20 included in the components of rate base for 00-0340?

21 A. As I mentioned previously, at the time  
22 that we filed the rate case, we had those costs under

1       appeal and they were included in rate base. The  
2       Company believed those were legitimate costs and still  
3       believes they are and they are still subject to  
4       recovery under appeal.

5                       They were identified as a line item in  
6       rate base. It was very easy for anyone reviewing that  
7       exhibit and also reviewing our testimony to understand  
8       exactly what those costs were and what they were  
9       related to. We had at least one question and answer  
10      in testimony describing what those costs were and why  
11      we included them in rate base.

12                     So the evidence was very clear in the  
13      testimony. It would have been very easy for Staff to  
14      understand why those costs were in there. And we  
15      believe and still believe that they are legitimately  
16      recoverable costs and are subject to recovery under  
17      the appeal.

18                     Q. From your answer I understand that, yes,  
19      they were intentionally included?

20                     A. Yes, they were included and, yes, they  
21      were intentionally included and were not concealed  
22      from review by anybody. As I say, we described

1 directly in testimony what those costs were related  
2 to.

3 Q. Did the Illinois-American Water Company  
4 request a stay of the Commission Order in 99-0418?

5 A. I don't know.

6 MS. VON QUALEN: That's all the questions I  
7 have.

8 EXAMINER SHOWTIS: I just had one question.

9 RE-EXAMINATION

10 BY EXAMINER SHOWTIS:

11 Q. Going back to Exhibit 3.5R, assuming  
12 those figures turn out to be accurate in terms of  
13 what's demonstrated with regard to savings, on a net  
14 present value basis what is the percentage of  
15 demonstrated savings that would be applied to recovery  
16 of the acquisition premium revenue requirement as  
17 compared to the percentage of savings that would flow  
18 through to customers? And when you provide the  
19 answer, could you tell me how you calculated that?

20 A. The answer is on the schedule 69.5  
21 percent or approximately 70 percent of the savings  
22 would go to cover the premium revenue requirement.

1 And as I mentioned previously, it doesn't cover the  
2 full cost of the investment made by the Company. The  
3 remaining approximately 30 percent goes to -- well,  
4 69.5 percent goes to cover the premium revenue  
5 requirement. Of the remainder, the majority of the  
6 remainder goes to customers. And that, the amount of  
7 the remainder that goes directly to customers, is 20  
8 percent.

9 Q. And where does the remaining 11.5 percent  
10 go?

11 A. The remainder is split 50/50 between --  
12 let me back up for a minute. Ten percent goes  
13 directly to customers and that's represented by Column  
14 7. The remaining 20 percent is split 50/50 between  
15 ratepayers and shareholders. And to derive those  
16 calculations I looked at total savings in Column 1  
17 which is 80 million, and to determine the portion that  
18 goes to recover the revenue requirement I divided the  
19 number in Column 5, 55.8 million, I divided that by 80  
20 million.

21 Q. And where was that figure? Is that the  
22 69.5?

1           A.   Correct.

2           Q.   And then that goes to the shareholders.

3       Okay, now account for the other 30.5.

4           A.   The Column 7 is ten percent of the first  
5       ten percent of savings which go to ratepayers and that  
6       is 8 million. That's essentially ten percent of the  
7       80 million in Column 1. And the remaining 20 percent,  
8       the remaining 20 percent is reflected by what's shown  
9       in Column 6. Column 6 only reflects 50 percent of the  
10      remainder.

11          Q.   So that would be an even split?

12          A.   Right. So essentially there is 16  
13      million remainder, 50 percent of which is shown in  
14      Column 6.

15          Q.   So then would the approximately 80  
16      percent of the savings flow through to stockholders,  
17      much of which would be used to cover the premium  
18      revenue requirement, and then 20 percent would flow  
19      through to ratepayers?

20          A.   Essentially, that's correct. Twenty  
21      percent would flow to ratepayers and the other 80  
22      percent would recover a majority of the investment

1       made by the shareholders to obtain the savings. The  
2       shareholders would not be recovering their full  
3       investment from that 80 percent.

4               EXAMINER SHOWTIS: Thank you. That's all I  
5       have.

6               MR. SPRINGER: Mr. Examiner, I do have a  
7       brief follow-up to the question you just asked, if I  
8       might.

9               EXAMINER SHOWTIS: As long as it pertains to  
10      the figures. If it's something besides the figures, I  
11      think it's -- I just asked for the calculation.

12              MR. SPRINGER: Well, per my question I think  
13      it does relate to it.

14                       REDIRECT EXAMINATION

15              BY MR. SPRINGER:

16              Q. Mr. Stafford, you were just asked by the  
17      Hearing Examiner about the percentage of savings that  
18      would be realized by ratepayers, if I understood the  
19      question, as compared to the portion of savings that  
20      would be utilized to cover the acquisition revenue  
21      requirement. Can you tell me, in the event that the  
22      acquisition revenue requirement was not incurred as a

1 result of the lack of the transaction being  
2 consummated, what level of savings would be realized  
3 by ratepayers in that event?

4 A. Ratepayers would see zero percent  
5 savings, zero dollars of savings.

6 MR. SPRINGER: Thanks. That's all the  
7 questions I have.

8 EXAMINER SHOWTIS: That's fine. I don't have  
9 any problem with that question. You can step down.

10 MR. SPRINGER: Our next witness will be  
11 Mr. Ruckman.

12 FREDERICK L. RUCKMAN  
13 called as a Witness on behalf of Illinois-American  
14 Water Company, having been first duly sworn, was  
15 examined and testified as follows:

16 DIRECT EXAMINATION

17 BY MR. SPRINGER:

18 Q. Please state your name and business  
19 address.

20 A. Frederick L. Ruckman, Illinois-American  
21 Water Company, 300 North Water Works Drive,  
22 Belleville, Illinois.

1           Q. And, Mr. Ruckman, by whom are you  
2 employed?

3           A. Illinois-American Water Company.

4           Q. And what is your position with that  
5 company?

6           A. Vice president and treasurer.

7           Q. Mr. Ruckman, have you prepared testimony  
8 for purposes of this case?

9           A. Yes, I have.

10          Q. I show you what's been marked for  
11 identification as IAWC Exhibit 2.0 and ask if that is  
12 direct testimony that you prepared?

13          A. Yes, it is.

14          Q. And in that testimony do you sponsor IAWC  
15 Exhibits 2.1 and 2.2?

16          A. Yes.

17          Q. Do you also sponsor in this case rebuttal  
18 testimony marked as Exhibit 2.0R?

19          A. Yes, I do.

20          Q. And in that testimony do you sponsor  
21 Exhibits 2.1R, 2.2R and 2.3R?

22          A. Yes.

1           Q. Do you also in this case sponsor  
2 surrebuttal testimony marked as Exhibit 2.0SR?

3           A. Yes.

4           Q. And in that testimony do you sponsor  
5 what's marked as Exhibit 2.4SR?

6           A. Yes, I do.

7           Q. And is the information contained in each  
8 of your testimonies and exhibits true and correct to  
9 the best of your knowledge?

10          A. Yes.

11          MR. SPRINGER: At this time, Mr. Examiner, I  
12 would ask for admission of Mr. Ruckman's direct  
13 testimony, Exhibit 2.0; the exhibits he sponsors in  
14 that testimony, Exhibits 2.1 and 2.2; Mr. Ruckman's  
15 rebuttal testimony, Exhibit 2.0R; and Exhibits 2.1R,  
16 2.2R and 2.3R that he sponsors in that testimony; and  
17 Exhibit 2.0SR, Mr. Ruckman's surrebuttal testimony;  
18 and Exhibit 2.4SR that he sponsors in that testimony.

19          EXAMINER SHOWTIS: Is there any objection?

20          MR. FITZHENRY: No.

21          EXAMINER SHOWTIS: Those exhibits are  
22 admitted into evidence.

1 (Whereupon IAWC Exhibits 2.0,  
2 2.1, 2.2, 2.0R, 2.1R, 2.2R,  
3 2.3R, 2.0SR, 2.4SR were  
4 admitted into evidence.)

5 MR. SPRINGER: Thank you. Mr. Ruckman is now  
6 available for cross examination.

7 CROSS EXAMINATION

8 BY MR. FITZHENRY:

9 Q. Hello, Mr. Ruckman. You were asked to  
10 provide a detailed numerical example illustrative of  
11 the apportionment of the acquisition adjustment and  
12 acquisition savings in IIWC Data Request Number 1,  
13 were you not?

14 A. I believe that's right, yes.

15 Q. I would like to ask you some questions  
16 about that response and I think it will be easier to  
17 follow as a cross examination exhibit, IIWC Exhibit 1.

18 (Whereupon IIWC Cross Exhibit 1  
19 was marked for purposes of  
20 identification as of this  
21 date.)

22 Q. Have I given you your responses to IIWC

1 Data Request Number 1 which has been marked for  
2 identification as IIWC Cross Exhibit Number 1?

3 A. Yes.

4 Q. And was it your intention that this  
5 exhibit would depict how the Shared Savings Plan would  
6 operate and how the acquisition premium and the  
7 acquisition savings would be apportioned throughout  
8 the 40-year plan period?

9 A. Yes, it was.

10 Q. So I am just going to ask you how you  
11 worked through the numbers. And let's start with year  
12 one, okay?

13 A. Sure.

14 Q. Under the column titled "Cost of Service"  
15 there is a line for cost of service without  
16 acquisition. And under your one it's \$150 million,  
17 correct?

18 A. Yes.

19 Q. First tell me, how did you arrive at the  
20 \$150 million figure?

21 A. It's an estimate of the total, a rough  
22 estimate, of the total revenue requirement of

1 Illinois-American plus the Citizens' properties.

2 Q. And so for in subsequent year 5, year 10,  
3 year 15, those are assumed figures based on your  
4 assumption as to what the cost of service would be for  
5 the combined companies in year one, is that right?

6 A. Yes.

7 Q. Now, then there is a line titled  
8 "Acquisition Savings Total per IAWC Exhibit 3.5,"  
9 correct?

10 A. Yes.

11 Q. And under your one again there is the  
12 figure \$3,717,638. That represents, according to  
13 Mr. Stafford's exhibit, what the demonstrated savings  
14 will be in year one after the acquisition, correct?

15 A. Yes.

16 Q. And so what you have done there on the  
17 third line is to subtract from the cost of service,  
18 the cost of service for the combined companies, the  
19 acquisition savings to arrive at the figure  
20 \$146,282,362, correct?

21 A. Yes.

22 Q. So the figure that I just mentioned is

1 the reduced cost of service that takes into account  
2 the demonstrated savings in year one?

3 A. Yes.

4 Q. In the next column or description of  
5 figures it is a calculation of net demonstrated  
6 savings. What you have done here is then to take the  
7 year one demonstrated savings of \$3.78 and then under  
8 the SSP the Company's proposal would be to take ten  
9 percent of that amount and that would be allocated to  
10 ratepayers, correct?

11 A. Yes.

12 Q. Now, the difference, the \$3,345,874, then  
13 gets added back to the cost of service for the  
14 combined companies, less the year one demonstrated  
15 savings, correct?

16 A. Yes.

17 Q. And that -- you have titled it "Adjusted  
18 Revenue Requirement" but that dollar amount is  
19 \$149,628.236, correct?

20 A. \$149 million.

21 Q. 628,000?

22 A. Right.

1           Q. And that would be the cost of service for  
2     ratemaking purposes in the event there was a rate case  
3     filed in that year one?

4           A. Correct.

5           Q. And so there is no examination of the  
6     Company's cost of service on a stand-alone basis in  
7     your exhibit or IIWC Cross Exhibit 1 whatsoever,  
8     correct?

9           A. That's correct.

10          Q. Now, if we look over at your 15, instead  
11     of just going through everything that I just went  
12     through with you, but if we look under the column  
13     titled "Calculation of Adjustment to Revenue  
14     Requirement" in year 15 what has happened is that the  
15     demonstrated savings are in such amount that it  
16     exceeds the acquisition premium in that year, correct?

17          A. That is correct, yes.

18          Q. And under the Company's SSP, the amount  
19     that exceeds the acquisition premium or acquisition  
20     adjustment, 50 percent would be allocated to  
21     ratepayers and 50 percent to shareholders, correct?

22          A. Yes.

1           Q. And there it shows again under year 15 in  
2           this particular column, that amount, the \$432,430,  
3           which is 50 percent of the excess demonstrated savings  
4           over the acquisition premium, is again added back into  
5           the cost of service, correct?

6           A. Yes.

7           Q. Now I would like you to look at your  
8           Exhibit 2.4SR.

9           A. Okay.

10          Q. First of all, do I understand that this  
11          exhibit was developed in response to certain testimony  
12          evidence offered by Staff witness Tom Smith?

13          A. That's correct.

14          Q. In the section that's titled "Calculation  
15          of Revenue Requirement," am I correct in understanding  
16          that you have shown here the manner in which the SSP  
17          would operate pretty much in the same way that we just  
18          went through in IIWC Cross Examination Exhibit 1 with  
19          the exception of in IIWC Cross Examination Exhibit 1  
20          you have also demonstrated the ten percent  
21          demonstrated savings that would go to ratepayers and  
22          you have also calculated the acquisition premium and

1       how it would be allocated?

2               A.   Yes.

3               Q.   Now I would like you to look at  
4       Mr. Smith's Exhibit 7.0, Schedule 1, if you could. Do  
5       you have a copy of that?

6               A.   Not before me, no. This is 7.0, Schedule  
7       1.

8               Q.   Page 1 of 3.

9               A.   Yes.

10              Q.   All right. And my question is just  
11       trying to understand what you have reflected on IIWC  
12       Cross Examination Exhibit 1 and your Exhibit 2.4SR  
13       with what Mr. Smith has shown here on his Exhibit 7.0,  
14       Schedule 1.

15              Mr. Smith would add back in as part of  
16       the cost of service for the combined companies the net  
17       demonstrated savings. By net demonstrated savings I  
18       mean the demonstrated savings in the year, less ten  
19       percent which would be allocated to ratepayers, and  
20       then added that difference to the cost of service for  
21       the combined companies to arrive at the total revenue  
22       requirement, is that correct? Is that how you

1 understand his schedule?

2 A. His schedule does that but it misses the  
3 point that --

4 Q. Well, I just really want to understand  
5 what you understand about how the schedule works  
6 mechanically as compared to what your schedules do  
7 mechanically. And I know that you have arguments and  
8 differences of agreement, but that's sort of a  
9 different issue, okay?

10 A. Okay.

11 Q. Now, if I go back to look at what you did  
12 in IIWC Cross Examination Exhibit 1, you would not  
13 have added back in as part of the cost of service for  
14 the combined companies the net demonstrated savings?

15 A. Repeat the question. I'm sorry.

16 Q. Again, it looks mechanically that on  
17 Mr. Smith's Schedule 7.0, Schedule 1, he has taken ten  
18 percent of the demonstrated savings and taken that  
19 difference and added that back into the cost of  
20 service for the combined companies to arrive at a  
21 total revenue requirement.

22 A. That is correct.

1           Q. Now, looking at IIWC Cross Examination  
2 Exhibit 1, what you have done is to --

3           EXAMINER SHOWTIS: Would you read back that  
4 prior question?

5                               (Whereupon the requested portion  
6 was then read back by the  
7 Reporter.)

8           EXAMINER SHOWTIS: Mr. Fitzhenry, when you  
9 talk about total revenue requirement, are you  
10 referring to line 13?

11          MR. FITZHENRY: Yes, sir, on Mr. Smith's  
12 exhibit.

13          EXAMINER SHOWTIS: It looks like to me,  
14 unless I am missing something, he added back in 90  
15 percent of the demonstrated savings on line 12 to get  
16 to the figure on 13, and you said ten percent.

17          MR. FITZHENRY: Well, ten percent from the  
18 demonstrated savings is, as I termed the net  
19 demonstrated savings, would be 90 percent of the  
20 demonstrated savings.

21          EXAMINER SHOWTIS: Okay, go ahead.

22          Q. Now, look at what you did on IIWC Cross

1 Examination Exhibit 1. What you have done is take the  
2 demonstrated savings and reduced the cost of service  
3 for the combined companies in year one by ten percent  
4 of that amount, correct?

5 A. Effectively, yes.

6 Q. Effectively.

7 A. And may I point out why my schedule is  
8 different than Mr. Smith's?

9 Q. Well, only because I know that Mr. Boyd  
10 Springer will do so. But, yes, go ahead.

11 MR. SPRINGER: I was thinking about it.

12 A. Well, I think what the discussion thus  
13 far has missed is the most important difference. The  
14 allocation of the demonstrated savings we are doing  
15 the same way, I believe. The basic premise that  
16 Mr. Smith's schedule misses is the fact that those  
17 demonstrated savings reduce the combined  
18 pre-acquisition revenue requirement. And that's not  
19 clear on his schedule. He is starting out with a  
20 hundred million. And that schedule in isolation, his  
21 schedule, says that after the Savings Sharing  
22 Proposal, the revenue requirement actually increases

1       by four and a half, almost five million dollars. And  
2       in my schedule that's not true. My schedule actually  
3       shows a reduced revenue requirement, and that's the  
4       whole point of our Savings Sharing Plan.

5               Q. I am not asking you to agree with  
6       Mr. Smith or Mr. Gorman for that example, but he takes  
7       the position he does because he believes that the  
8       acquisition premium becomes part of the cost of  
9       service for the combined companies.

10              A. The acquisition premium indirectly  
11       becomes a part of the cost of service, but the overall  
12       cost of service is still below what it was on a  
13       pre-acquisition basis.

14              Q. At your direct testimony, in your direct  
15       testimony at page 7, you indicate that the present  
16       value of the acquisition of savings is approximately  
17       \$76.2 million?

18              A. Yes.

19              Q. Now, should that number show up on  
20       Mr. Stafford's Exhibit 3.5?

21              A. I believe that there was an original 3.5  
22       that was later replaced with a revision 3.5R. So it's

1       very possible that number came from the original  
2       exhibit.

3               Q.   Okay.  If you could, would you look at  
4       Mr. Stafford's Exhibit 3.5R and then tell me if the  
5       \$76.2 million number should have changed?

6               A.   I believe that would now be 80 million.

7               Q.   Likewise, on the next page of your direct  
8       testimony you indicate that the acquisition premium or  
9       acquisition adjustment is \$66.6 million.  Would that  
10      number be reflected now on Mr. Stafford's Exhibit  
11      3.5R?

12              A.   I don't think that number actually shows  
13      on 3.5R.

14              Q.   Under Column 3 of Mr. Stafford's Exhibit  
15      3.5R does that not show the total premium revenue  
16      requirement of net present value or present value of  
17      75.7 million?

18              A.   Yes, but that is not directly the same  
19      number as the acquisition premium.

20              Q.   Is there any -- so you are saying that  
21      there is nothing on Mr. Stafford's Exhibit 3.5R that  
22      is the acquisition adjustment referred to on page 8 of

1 your testimony?

2 A. That's right.

3 Q. If we were to look at this just on a net  
4 present value basis where you have Synergy savings of  
5 \$80 million and an acquisition adjustment to be  
6 recovered of \$66 million, again on a present value  
7 basis is the \$14 million what is at issue here?

8 A. If you are comparing -- I'm sorry, 80 to  
9 what?

10 Q. Sixty-six.

11 A. Oh, the \$66 million. Is that what's at  
12 issue?

13 Q. Yes. I mean, you are going to spend \$66  
14 million to save \$80 million?

15 A. We are going to spend -- we are going to  
16 incur an acquisition premium and we are going to  
17 produce for ratepayers a savings over 40 years of  
18 approximately \$16 million net present value.

19 Q. \$16 million?

20 A. \$16 million for that period.

21 Q. Now, you have heard me ask questions of  
22 other IAWC witnesses about the savings back to IAWC,

1       and I believe everybody agrees that it will be  
2       approximately 4.5 percent. Do you remember those  
3       questions and those answers?

4               A. Yes.

5               Q. And if we were to look again at the \$16  
6       million difference between the Synergy savings and the  
7       acquisition adjustment to be recovered and look at on  
8       a net present value basis what this means to IAWC  
9       ratepayers, would you agree subject to check that 4.5  
10      percent of \$16 million is approximately \$720,000?

11              A. Subject to check. I don't quite get what  
12      the point is.

13              MR. FITZHENRY: Thank you. That's all the  
14      questions I have. I move for the admission of IIWC  
15      Cross Examination Exhibit 1.

16              MR. SPRINGER: No objection.

17              EXAMINER SHOWTIS: IIWC Cross Exhibit 1 is  
18      admitted.

19                                      (Whereupon IIWC Cross Exhibit 1  
20                                      was admitted into evidence.)

21              EXAMINER SHOWTIS: Has the reporter been  
22      given a copy to mark?

1 MR. FITZHENRY: Three.

2 EXAMINER SHOWTIS: We only need one.

3 MR. CLENNON: Staff has some questions.

4 EXAMINER SHOWTIS: Go ahead.

5 MR. CLENNON: May I proceed?

6 EXAMINER SHOWTIS: Yeah.

7 MR. CLENNON: Thank you.

8 CROSS EXAMINATION

9 BY MR. CLENNON:

10 Q. Good afternoon, Mr. Ruckman.

11 A. Good afternoon, Mr. Clennon.

12 Q. I am going to try a little different with  
13 you and perhaps am going to look at my notes and see  
14 if we can't get off to a good start here. If you  
15 could turn to page 11 on your direct testimony?

16 A. Yeah.

17 Q. And then on the question and answer that  
18 begins on line 11 you talked about the -- this is the  
19 five-year dates with the report or proposed rates. Is  
20 that the subject matter of the testimony here?

21 A. Yes.

22 Q. So if I understand what this says, is

1       that five years from now there will be a proceeding  
2       and there will either be rates reflecting the level of  
3       the savings or there will be some kind of report  
4       describing what those savings are to the Commission?

5               A.   Correct.

6               Q.   Now, is it true that you expect all of  
7       the savings to occur within a -- a majority of the  
8       savings to occur within a year?

9               A.   Shortly after the acquisition, yes.

10              Q.   Shortly after the acquisition.  So, for  
11       example, if those savings were \$10, there would be  
12       five years before the ratepayers would ever see those,  
13       is that accurate?

14              A.   It would be five years before they would  
15       be reflected in new rates.

16              Q.   Okay.  And so for five years the Company  
17       would be collecting the \$10?

18              A.   That would be used to offset any  
19       otherwise revenue deficiency that the Company might  
20       have.

21              Q.   Okay.  Now, there was some discussion  
22       about that revenue deficiency and it's my

1 understanding that Illinois-American is going to come  
2 in with a rate case sometime this year, is that true?

3 A. Of course, for the existing Citizens.

4 Q. For the Citizens Company?

5 A. It's possible, yes.

6 Q. Do you know what kind of test year is  
7 going to be used?

8 A. Haven't decided that, no.

9 Q. It's possible it could be a historical  
10 test year?

11 A. Could be.

12 Q. And that would be permitted?

13 A. Yes.

14 Q. And then that would reflect a level of  
15 costs prior to the savings?

16 A. Possibly.

17 Q. Okay.

18 EXAMINER SHOWTIS: When you state possibly,  
19 under what circumstances would it not reflect a level  
20 of costs prior to the savings? In other words, if you  
21 came in, filed a rate increase request for the  
22 Citizens' service territory based on an historic test

1       year, would you tell me under what circumstances that  
2       would reflect a level of costs that incorporates any  
3       savings?

4               THE WITNESS:  It probably would not.

5               EXAMINER SHOWTIS:  So when you said possibly,  
6       you can't think of a circumstance right now where it  
7       would?

8               THE WITNESS:  Correct.

9               MR. CLENNON:

10              Q.  Could you turn to page 9 of your direct  
11       testimony?  And the sentence that begins on line 29,  
12       "The Company is proposing that the order issued in  
13       this proceeding explicitly authorize recovery of the  
14       acquisition adjustment in accordance with the home  
15       mortgage method of amortization subject to  
16       demonstrating that savings exceed revenue requirements  
17       relating to the amortization of the acquisition  
18       adjustments."  And that ends that page.  That may not  
19       be a perfect reading but is that a fair reading of  
20       your testimony?

21              A.  I am sorry, Mr. Clennon, what page did  
22       you say?

1           Q. It was on page 9, beginning on line 29,  
2 going to the first line of page 10.

3           EXAMINER SHOWTIS: Have you got the right --

4           THE WITNESS: Yes.

5           MR. CLENNON: Do I have the right one?

6           MS. SCHULTZ: Yes.

7           Q. Is it your testimony that under 7-204 the  
8 Company is only asking the Commission to allow  
9 recovery of the acquisition adjustment? Is that the  
10 only cost you are asking for in this case?

11          A. The Company is asking to share in the  
12 savings that are generated as a result of the  
13 acquisition. And that sharing, through that sharing,  
14 the Company is compensated for the investment it makes  
15 to produce those savings.

16          Q. Okay. Just so I understand, you have  
17 identified a cost, call it merger premium, acquisition  
18 adjustment, right? You have put together a proposal  
19 to, for lack of a better word, extract the money to be  
20 compensated for that, for the ratepayers to pay you  
21 for that, for that one cost, and that is the cost you  
22 are seeking the Commission's approval on in this

1 proceeding?

2 A. Again, we are -- our plan, our Savings  
3 Sharing Proposal, is a methodology to share savings,  
4 on the one hand to provide benefits through savings to  
5 customers, and on the other hand to provide a  
6 mechanism for the Company to be compensated for the  
7 acquisition premium that it's incurred.

8 Q. Mr. Ruckman, that's a perfectly  
9 legitimate answer to my question. I am really  
10 concerned about the costs that you have identified and  
11 which you are seeking recovery for in this proceeding.

12 MR. SPRINGER: Is there a question?

13 EXAMINER SHOWTIS: Let me try to shorten  
14 this. I have been involved in some proceedings where  
15 a premium is identified and then there is so-called  
16 transition costs, costs that would be -- besides the  
17 premium there is certain costs that utilities say are  
18 necessary to achieve the savings. They have to incur  
19 costs in certain areas in order to achieve the  
20 savings.

21 I think what Mr. Clennon's driving at is  
22 I didn't see anything in the record or hear about such

1 transition costs, that if you want to call the  
2 acquisition premium or acquisition adjustment a cost,  
3 I think he was asking you is that the only cost for  
4 which some recovery is sought in this proceeding, that  
5 is, there is not separately identified transition  
6 costs or other costs.

7 THE WITNESS: That is true. We would  
8 classify that as an asset on the balance sheet. But  
9 that is the only -- there is no other transaction type  
10 costs that we are seeking recovery of.

11 MR. CLENNON:

12 Q. Are there any other costs associated with  
13 the merger that the Company seeks to recover?

14 A. No.

15 Q. If you could go to page 6, sir, and the  
16 question beginning on 7 where you talk about the  
17 capitalization structure after the financing, that  
18 question and answer, would this question and answer  
19 change in light of this promise not to increase the  
20 cost of or the overall rate of return due to the  
21 merger that we heard about yesterday?

22 A. Well, that promise that you allude to

1       that was made yesterday was really not addressing the  
2       overall capital structure as much as it was addressing  
3       under the particular scenario that was being discussed  
4       which was the Commission approves the Company's  
5       Savings Sharing Plan but the Company is unable to  
6       demonstrate any savings. There could, from that,  
7       potentially be a marginal increase in the Company's  
8       cost of capital, and the Company has said that it  
9       would not seek in a rate proceeding that incremental  
10      increase in capital.

11               That is the promise that was made. I  
12      don't believe that had anything really to do with the  
13      capital structure so much as the overall cost of  
14      capital.

15              Q. Okay. But just so I understand, but that  
16      overall cost of capital will be affected in some way  
17      or no, is that your testimony?

18              A. Under what?

19              Q. Under this, for lack of a better word,  
20      the Flaherty promise?

21              A. I want to make it clear that is not a  
22      Flaherty promise. That is a Company promise.

1                   MR. FITZHENRY: Flaherty will get you  
2   nowhere.

3                                   (Laughter)

4                   THE WITNESS: Is there a question  
5   outstanding?

6                   Q. Who does Mr. Flaherty work for, by the  
7   way?

8                   A. Deloitte and Touche.

9                   Q. Has anyone from the Company made that  
10   promise in testimony?

11                  A. Yes, not in testimony but in a data  
12   request actually.

13                  Q. Are you in a position to make that  
14   promise here on the stand?

15                  A. Absolutely. I think it's already on the  
16   record, isn't it? I just said it, did I not?

17                  Q. Very good. You are familiar with the  
18   rate case that is currently underway here at the  
19   Commission for Illinois-American Water Company, are  
20   you?

21                  A. Yes.

22                  Q. Now, I have a copy of the brief on

1 exceptions filed by the Company in that case. And on  
2 page 2 it says that it's a summary of the Company's  
3 positions and it talks about the rate of return on  
4 common equity. And this is just a little blurb, I  
5 will be happy to show it to you, I think I can read  
6 the whole paragraph. It says under the subtitle of  
7 (A) Rate of Return on Common Equity, it says, "The  
8 Company has requested a rate of return on common  
9 equity of 11.25 percent. Its expert witness Paul  
10 Mulle supports a higher rate. However, the Company  
11 proposes 11.25 to mitigate rate impacts on its  
12 customers."

13 So if I understand the Company's position  
14 in the rate case, that rate of return on common equity  
15 should be higher, hence should be higher than what was  
16 proposed by the Company, and even higher than what the  
17 HEPO, which may or may not be passed by the  
18 Commission, suggests. That would lead to a higher  
19 rate of return -- I'm sorry, yeah, that would lead to  
20 a higher rate of return which you may not get, which  
21 you will not get, and you have not asked for, is that  
22 accurate?

1           A. Yes.

2           Q. So you are going to forego the higher  
3 rate of return in the rate proceeding and then forego  
4 a higher rate of return which you may be entitled to  
5 in order to get the transaction consummated, is that  
6 right?

7           A. I don't see the connection then. That  
8 rate case -- what I am saying is that in the rate case  
9 our expert witness supported a higher rate of return  
10 than the Company requested when it put together its  
11 filing.

12          Q. Okay. So just so I understand, there is  
13 a higher rate of return that was demonstrated and a  
14 higher one could have been asked for by the Company?

15          A. Yes.

16          Q. That's one of them. In addition to that,  
17 in the future the Company may be entitled to a higher  
18 rate of return but has agreed through the promise, I  
19 guess we could call it the Ruckman promise now, not to  
20 seek that higher rate of return?

21          A. I think there is -- in my view there is a  
22 disconnect here.

1           Q. I am not asking you to connect them. I  
2           want to make sure that the facts are clear, that my  
3           understanding of things is correct.

4           A. Well, what the Ruckman promise is, what  
5           the Illinois-American promise is, is that under the  
6           scenario that's described, the Commission approves the  
7           Company's Savings Sharing Proposal. And in the  
8           unlikely event that the Company is unable to  
9           demonstrate those savings, which we think is a totally  
10          not possible scenario, but in that event, hypothetical  
11          event, the Company's overall cost of capital, debt  
12          capital, would be marginally higher. And we would not  
13          ask in a future rate proceeding for that marginally  
14          higher increase in cost of capital as a result of the  
15          financial impairment that has occurred to the Company  
16          because of its inability to recover any of its  
17          investment in the Citizens Company.

18          Q. I understand that. So that coupled with  
19          the reduction on the overall rate of return agreed to  
20          by the Company in the rate case would be two factors  
21          reducing the Company's overall rate of return, as I  
22          see it. Is that an accurate statement?

1           A. The overall rate of return that was  
2 requested or allowed in this rate case is a rate of  
3 return in this case on equity that is set, essentially  
4 re-set, every rate case.

5           Q. Right.

6           A. And in the next rate case that the  
7 Company would file that rate of return would be set  
8 again. And who

9           Q. So perhaps only with -- I'm sorry, sir, I  
10 didn't mean to cut you off.

11          A. I didn't really say anything more. Who  
12 knows where it will be set at that time.

13          Q. But there may be some overlap, isn't that  
14 right?

15          A. I don't know what overlap there would be.

16          Q. Okay. Well, perhaps there would be  
17 overlap because you are going to file another rate  
18 case here in a year, within a year?

19          A. For the Citizens' property.

20          Q. Yeah. You used to work for NI Water, is  
21 that correct?

22          A. Yes.

1           Q. When did you become employed by  
2 Illinois-American Water?

3           A. January 1 of 2000.

4           Q. And was there an event that led to your  
5 employment there in Illinois-American Water Company?

6           A. Yes.

7           Q. What was that?

8           A. I was promoted to the position of vice  
9 president/treasurer of Illinois-American.

10          Q. Was this after the merger with NI Water?

11          A. It was actually just before. I think the  
12 merger was consummated in April or thereabouts.

13          Q. Was your position secured by the terms  
14 and conditions of the merger?

15          A. No.

16          Q. No?

17          A. Not that I am aware of.

18          Q. Would you describe your employment at  
19 Illinois-American Water Company as a direct result of  
20 the merger with NI Water?

21          A. It would not otherwise have happened had  
22 that merger not taken place.

1           Q. Now, nothing personal, but are you an  
2 example of added bureaucracy after a merger?

3           A. I am not going to admit to that.

4                               (Laughter)

5           Q. Okay. That's fine. All right. Now  
6 let's get down to some serious work. Mr. Ruckman, I  
7 notice prior to you coming to work at  
8 Illinois-American Water Company you worked at NI Water  
9 as an accountant, is that right?

10          A. Yes.

11          Q. You are not an attorney at law, are you?

12          A. No.

13          Q. Did you ever attend law school?

14          A. No.

15          Q. In your direct testimony you make a  
16 reference to the Union Electric Company versus  
17 Illinois Commerce Commission, that's on page 12, I  
18 believe, isn't that correct?

19          A. Yes.

20          Q. When you gave that testimony, wasn't it  
21 your intention to provide a legal opinion?

22          A. No.

1           Q. So when you are referring to the statute  
2 and case law, you are doing so as a lay person?

3           A. Yes.

4           Q. Sir, did you prepare this portion of your  
5 testimony yourself?

6           A. Not the legal cites, no.

7           Q. So did you do so with the advice of  
8 counsel?

9           A. Yes.

10          Q. Now, on page 12 of the testimony there is  
11 a cite to the Union Electric case beginning on line 22  
12 and going to about half way through on line 24. Do  
13 you know where in the case that quotation comes from?

14          A. I have looked at that case and found  
15 approximately where that appears, yes.

16          Q. Can you tell me where that quote comes  
17 from?

18          A. Page 377.

19          Q. Can you tell me the beginning of the  
20 paragraph that you are referring to?

21          A. "The first argument contends that in  
22 these cases the Commission" --

1           EXAMINER SHOWTIS: Maybe to shorten this, I  
2     think any citations to cases or arguments, although  
3     cases I think maybe are best left for the briefs, and  
4     Mr. Ruckman's layman's position as to what a case  
5     means, I don't think should be given any weight. So I  
6     don't think I want to waste time arguing over whether  
7     he is interpreting a case correctly or incorrectly  
8     because, as I said in other proceedings, I think the  
9     weight should only be given to the arguments that the  
10    attorneys provide in the briefs that are filed and not  
11    to a witness' statement as to what a case means.

12           MR. CLENNON: Okay. That's fine.

13           EXAMINER SHOWTIS: This might shorten it, but  
14    I don't see the purpose in arguing with this witness  
15    over something that must have been provided to him  
16    anyway by counsel for purposes of his testimony, you  
17    know, what it means or whether you disagree with it.

18           MR. CLENNON: I will take care of it on a  
19    brief then, sir. If I could just ask one more  
20    question?

21           EXAMINER SHOWTIS: That's fine.

22           Q. In the rate case that we just talked

1       about for Illinois-American Water Company, what was  
2       the measure of rate base for that case? Was that fair  
3       value or was it original cost?

4               A. Original cost.

5               Q. Do you propose to change the methodology  
6       in your next case?

7               A. Do I?

8               Q. Yes.

9               A. I reserve the right to change it. But at  
10       this time probably not.

11              Q. Would you go to page 7 of your rebuttal  
12       testimony?

13              A. Yes.

14              Q. There I believe you begin discussing the  
15       acquisition savings, am I correct?

16              A. Yes.

17              Q. All right. Is it correct that a  
18       utility's costs represent liabilities which have been  
19       incurred?

20              A. Incurred and paid, among other things.  
21       That's not the total cost but --

22              Q. Is it correct to say that costs, just to

1 use your words, have been paid -- I'm sorry, let me  
2 start again. Is it correct to say that costs have  
3 been paid or you can prove that costs have been paid  
4 through the existence of documents such as invoices,  
5 contracts, things like that?

6 A. That's one way to prove costs, yes.

7 Q. Now, if I understand things correctly, is  
8 it correct that the acquisitions that you refer to  
9 represent the lack of costs, acquisition savings?

10 A. They represent exactly what we say. They  
11 represent what were costs that are no longer costs  
12 going forward.

13 Q. So they would be lighter costs?

14 A. Yes.

15 Q. If you could go to page 12, I think it's  
16 beginning on about line 3.

17 A. Yes.

18 Q. You state, "Illinois-American will limit  
19 the amount of revenue sought in each rate proceeding  
20 to the amount of demonstrated savings. The  
21 alternative ratemaking proposal would, therefore, have  
22 no adverse effects on rates at any time," is that

1 correct?

2 A. Yes.

3 Q. Fair reading?

4 A. Yes.

5 Q. Is my understanding correct that when you  
6 use the term "demonstrated savings," it indicates that  
7 Illinois-American Water Company does not intend to  
8 use -- does not intend to base its future rates on  
9 something -- let me start over. By the use of the  
10 term "demonstrated savings," am I to understand that  
11 Illinois-American Water Company in some future rate  
12 case is going to base the rates on something other  
13 than cost?

14 A. Illinois-American in a future rate case  
15 is going to demonstrate that the costs that -- are  
16 going to demonstrate two things. On the one hand they  
17 are going to demonstrate what the costs are and they  
18 are going to demonstrate what the savings are that  
19 have been generated as a result of the acquisition  
20 that takes place. And the revenue requirement is then  
21 going to be based on a combination.

22 Q. So it will be cost and lack of cost? Is

1       that a shrug maybe?

2               A.   It's going to be based upon a cost level  
3       that is less than -- we will demonstrate the cost  
4       level is less than it otherwise would have been absent  
5       the acquisition.

6               Q.   Once again, normally the utility, just  
7       generally speaking, you figure out all the costs, you  
8       figure out the revenue needed to cover those costs  
9       plus a little rate of return, very generally, and  
10      that's how rates are set, is that correct?

11              A.   Yeah.

12              Q.   Is it the Company's proposal to figure  
13      out what its costs are, right, including the  
14      acquisition adjustment, minus something, and that will  
15      be its total cost of providing service?  When you  
16      figure out the revenue, you add a little rate of  
17      return on?

18              A.   Can you read that back to me, please?

19                               (Whereupon the requested  
20                               portion was then read back by  
21                               the Reporter.)

22              MR. SPRINGER:  I don't think that question is

1       answerable.

2               Q.   I will try it again.   Just so I  
3       understand this SSP, you are going to have the cost of  
4       the combined companies, plus you are going to add the  
5       revenue, the acquisition revenue requirement merger  
6       premium, whatever you want to call it, and that's  
7       fine.   Then you are going to -- say it two ways.   You  
8       are going to subtract the savings or you are going to  
9       subtract some savings, or you are going to add  
10      negative costs, however you want to say it, and that's  
11      going to come up with your revenue requirement.   Do I  
12      understand it correctly?

13              A.   You said "however I want to say it."   Let  
14      me say how I would like to say it.

15              Q.   Sure.

16              A.   If the Company invested in any other  
17      utility plant, a million dollar utility plant, and  
18      maybe that utility plant is replacing an old obsolete  
19      utility plant that was inefficient, and by spending a  
20      million dollars we generated savings as a result of  
21      that.   When we came into a rate case there would be no  
22      question about whether or not we would be able to earn

1     on our million dollar investment, and those savings --  
2     those savings would be reflected in the revenue  
3     requirement.

4             The difficulty we have here is that this  
5     Commission generally does not allow a rate of return  
6     on an acquisition adjustment. And yet the Company is  
7     making an investment that is going to produce  
8     substantial savings. And the only way that we can  
9     recover our costs is through the Savings Sharing  
10    Proposal. And the way we are proposing to do that is  
11    to share the savings that we demonstrate to this  
12    Commission.

13            And by demonstrate I mean the Company  
14    puts together schedules that we believe will be  
15    auditable. I don't see any difficulty whatsoever in  
16    putting together those schedules. They will be  
17    subject to Commission Staff's review and ultimately to  
18    the Commission's approval. And the way the Company is  
19    made whole is through the sharing of those  
20    demonstrated savings. Otherwise, we wouldn't be  
21    talking about a Savings Sharing Proposal, if we were  
22    allowed to earn on our investment like we are other

1 utility investments.

2 Q. Okay. Let me just ask you this question.  
3 When you buy this investment that you have described,  
4 that produces a savings on -- I don't know a good  
5 example of one -- a super good pump, something like  
6 that. You have an invoice for that pump, is that  
7 correct?

8 A. Correct.

9 Q. Now, when you talk about providing  
10 schedules and proving to the Commission, it is my  
11 understanding that from time to time these schedules  
12 or information you are going to provide to this  
13 Commission is going to change at your whim, is that  
14 right? I asked the witness yesterday if for any  
15 reason the Company thought it may need to change the  
16 way this information was presented. That witness said  
17 sure, that would be acceptable. Your position today  
18 is that once the proposal is set in place, the Company  
19 will not deviate from it?

20 A. The proposal the Company has put in place  
21 is what the Company believes is fair to the Company  
22 and fair to the ratepayers and meets the standard of

1       7-204. And there has been no other proposal put  
2 before us in this proceeding.

3               Q. Let me rephrase my question. Is it your  
4 position today that when the Company has within five  
5 years figured out the means and methods on which it is  
6 going to track savings, that methodology is going to  
7 remain set?

8               A. Unless the Company and the Commission  
9 Staff were to agree upon some other methodology that  
10 both were happy with, yes, I would expect it would be  
11 set.

12              Q. Do you foresee a time when the Company  
13 and Staff would not agree on changing the methodology  
14 to demonstrate savings and the Company would bring  
15 that in front of the Commission?

16              A. When we would not agree?

17              Q. Yes, would not agree on the methodology  
18 to continue -- the Company believes a change is  
19 necessary. They present it to the Staff. The Staff  
20 does not agree. Is it your position right now that  
21 the Company is going to drop it there or is it your  
22 position that the Company would file a petition

1 seeking appropriate relief to change the methodology  
2 to determine a savings?

3 A. Well, I have no reason to speculate at  
4 this point in time that the Company would intend to  
5 change the methodology that we have before the  
6 Commission right now, unless it was really to respond  
7 to the Commission Staff's concerns about that  
8 methodology.

9 Q. It's my understanding Mr. Stafford just  
10 testified that there may be an event which would cause  
11 the Company to re-evaluate the nature of savings and  
12 that in the future there may be additional savings not  
13 known at this time and the Company would seek to have  
14 those savings shared 50/50 between the ratepayers and  
15 the stockholders. Are you saying that's not going to  
16 happen?

17 A. I frankly don't remember Mr. Stafford  
18 saying that.

19 Q. Okay. I believe what he said was the  
20 Company intends to keep track of certain costs. There  
21 may be an event which will have to re-establish or  
22 re-evaluate whether that cost affected the merger

1       savings -- I'm sorry, that event affected the merger  
2       savings? Did I understand it correctly?

3               A. Let me say what I recollect. And that is  
4       that we were talking about merger savings and we were  
5       talking about the fact also that the Company has  
6       recognized that there could be additional costs as a  
7       result of the merger, the five positions, as an  
8       example. And I think that discussion was simply a  
9       recognition of the fact in the Company's plan that it  
10      is comprised mostly of savings, but it is also  
11      recognized that we cannot absorb that customer base  
12      without having to have some additional staff, for  
13      example, customer service. We cannot absorb 70,000  
14      combined water and wastewater customers without having  
15      some addition to our customer service staff. And so  
16      we in our proposal netted those savings.

17             Q. So is it your position that the savings  
18      identified by Mr. Stafford will never be added to or  
19      subtracted from?

20             A. No.

21             Q. So the savings that are described by  
22      Mr. Stafford could in fact change?

1           A. Oh, I expect they will change, sure.

2           That is our -- that is simply our forecast right now  
3           of what we expect to happen. It hasn't happened. It  
4           will change.

5           Q. And not just the quantity of savings, but  
6           the categories of savings may in fact change?

7           A. They may.

8           Q. It's my understanding that the Company's  
9           position is that the acquisition adjustment reflects  
10          the market value of the utility as set at the time  
11          that it was purchased. Is that a fair recital?

12          A. The purchase price.

13          Q. The purchase price, okay. And the  
14          purchase price is determined by the market, is that  
15          correct?

16          A. Yes.

17          Q. So it would be the market value that  
18          determines the purchase price?

19          A. Purchase price is the market value, yes.

20          Q. It's my understanding that market values  
21          are constantly changing, is that true?

22          A. I would agree.

1 Q. Do you have a TQS-2.9?

2 A. Is that addressed to me? Yes, I do have  
3 it.

4 Q. All right. Somewhere in there -- I don't  
5 have it in front of me but I can dig it out if I need  
6 to. The Company's proposal is to allocate -- you  
7 state the Company's proposal is to allocate  
8 demonstrated savings as it would other non-functional  
9 costs. Is that a fair reading?

10 A. Yes.

11 Q. Is it my understanding that your position  
12 is that savings are costs?

13 A. Savings are foregone costs, yes.

14 EXAMINER SHOWTIS: Would you explain to me  
15 what -- I am not familiar with the term non-functional  
16 costs. Would you tell me what kind of costs you are  
17 talking about here?

18 THE WITNESS: Well, if you get into the  
19 detail of a cost of service study, the Commission  
20 Staff has a cost of service study model that allocates  
21 certain costs to certain areas such as production,  
22 customer costs, which would go into the facilities

1 charge. Then there are other kinds of costs.

2 EXAMINER SHOWTIS: Okay. I think I  
3 understand now. General costs that cannot be assigned  
4 to specific functions?

5 THE WITNESS: Right.

6 EXAMINER SHOWTIS: Okay.

7 BY MR. CLENNON:

8 Q. If we could go to your surrebuttal  
9 testimony, and I think it's on page 1, line 19?

10 A. Yes.

11 Q. You state, "Under the SSP rates would  
12 have been at or below the level which would exist in  
13 absence of the acquisition."

14 A. What page are we on?

15 Q. I believe it's page 1. I can triple  
16 recheck it. I have been having trouble with my pages.

17 A. I don't see that.

18 Q. I think it's on page 1, line 16, under  
19 the SSP, under the Savings Sharing Proposal.

20 A. What line?

21 Q. On my copy, sir, it's 16.

22 A. Okay, I am there.

1           Q. Okay. By this testimony are you stating  
2           that you currently know what the level of charges to  
3           Citizens' customers will be in the year 2040?

4           A. I am saying that I know that the charges  
5           would be less than they would otherwise be absent the  
6           acquisition.

7           Q. So in order to make that assertion you  
8           must have some idea then what the rates would be?

9           A. No, I don't have to know that. What I  
10          have to know is that currently the two companies both  
11          have duplicative staffs. We have two HR directors, we  
12          have two accounting departments, we have two  
13          information systems departments. And when we merge,  
14          there will no longer need -- there will no longer be  
15          the need to have two.

16          Q. And are you saying that the merger is the  
17          only way to reduce those costs?

18          A. Yes. Without the merger, those positions  
19          would still have to be there. Citizens stand-alone  
20          cannot function without a separate IS staff, HR  
21          department, accounting department. That's the whole  
22          thrust of the proposal.

1           Q. So in your mind over the next 40 years  
2 there is no event that would intervene to reduce those  
3 costs other than the merger?

4           A. I don't know what event there would be  
5 that would cause Citizens to be able to operate  
6 stand-alone without an HR department, without an  
7 accounting department, without an information systems  
8 department, and all those other duplicative positions  
9 that there now are. I don't know how that can happen.

10          Q. Could we go to Exhibit 2.4SR?

11          A. Yes.

12          Q. Now I want to just ask some -- get some  
13 clarifying questions here. So bear with me, a lot of  
14 numbers, things like that. So does line 1 reflect  
15 your assumed cost of operating Citizens without the  
16 acquisition by Illinois-American?

17          A. It assumes a stand-alone operation, yes,  
18 stand-alone operation of the two companies.

19          Q. All right. Is it your position that if  
20 Citizens is acquired by Illinois-American, that it  
21 will be possible to calculate the cost of operating  
22 Citizens in the year 2040 as if the acquisition did

1 not occur?

2 A. I don't really have an intention to  
3 calculate that. My intention is to demonstrate the  
4 level of savings on an ongoing basis that was  
5 generated as a result of the acquisition.

6 EXAMINER SHOWTIS: I think some of this has  
7 probably already been covered. If I recall, Mr.  
8 Stafford said it would not be the intention of the  
9 Company to do a complete cost of service study for  
10 Citizens as a stand-alone company through 2000 going  
11 out 40 years.

12 Q. Okay. If we could go to Scenario 1, line  
13 1, is it assumed that the revenue requirement without  
14 the acquisition is a hundred million?

15 A. Yes.

16 Q. And referring to Scenario 1, line 4, is  
17 it assumed that the savings from the acquisition is  
18 5,500,000?

19 A. Yes. And let me also make clear that  
20 these numbers were the -- I believe this is the  
21 Company's representation of a Staff schedule using  
22 their same numbers.

1           Q. Very good. Does it follow that the  
2 revenue requirement of Citizens as acquired by  
3 Illinois-American is \$94,500,000?

4           A. The ultimate revenue requirement of the  
5 two companies on a pre-acquisition basis is a hundred  
6 million and on a post-acquisition basis is \$99,450,000  
7 as shown on line 20.

8           Q. Could you skip down to line 17?

9           A. Sure.

10          Q. And what was your last answer to the  
11 question I asked? I'm sorry.

12          A. My answer was that on a pre-acquisition  
13 basis the combined revenue requirement of the two  
14 companies was a hundred million dollars as shown on  
15 line 1, and on a post-acquisition basis the combined  
16 revenue requirement of the two companies would be as  
17 shown on line 20, \$99,450,000, thus resulting in a  
18 reduced revenue requirement of \$550,000.

19          Q. I am wondering, sir, if you have an  
20 opinion as to whether or not it is necessary for  
21 General Motors to calculate the production cost of a  
22 year 2001 Oldsmobile as though General Motors had

1 never purchased Oldsmobile from Ransom E. Olds?

2 A. That's the Ransom Olds question. I have  
3 no opinion.

4 MR. CLENNON: Very good. Staff has nothing  
5 further.

6 EXAMINER SHOWTIS: I think, Mr. Ruckman,  
7 there are some advantages to being the last witness  
8 for the Applicants because I think quite a few of the  
9 questions that I was going to ask you have been  
10 answered.

11 THE WITNESS: Oh, go ahead.

12 EXAMINER SHOWTIS: No, I am trying not to  
13 repeat any question that has already been answered by  
14 a witness from the Applicants.

15 THE WITNESS: I appreciate that, although  
16 some of those questions I was wishing I could have.

17 EXAMINER SHOWTIS: Hold on a second. I am  
18 going through my questions. I think almost all of  
19 them have been answered by a witness previously.

20 MR. CLENNON: Your Honor, I was reminded by a  
21 Staff witness that I failed to ask a couple of  
22 clarifying questions. If the parties would leave, I

1 would ask permission with their leave to ask a couple  
2 questions.

3 EXAMINER SHOWTIS: Go ahead.

4 MR. CLENNON: I am sorry, Mr. Ruckman. I  
5 promise these won't hurt.

6 Q. On page 8 of your surrebuttal testimony,  
7 lines 14 to 16, you state you accept the ICC Staff  
8 Exhibit 10.1, Schedule 10.1, as the corrected version  
9 of the Illinois-American Water Exhibit 2.1R? Is that  
10 a fair reading?

11 A. Yes. Redirect me to the page number. I  
12 don't recall that.

13 Q. It's page 8 of your surrebuttal.

14 A. Yes, I do recall that.

15 Q. So it's my understanding then you accept  
16 Staff's Schedule 10.1?

17 A. Right.

18 Q. In its entirety?

19 A. Yes.

20 Q. Okay. In your opinion is  
21 Illinois-American Water's, stand-alone, current  
22 financial condition, given your analysis of its

1 financial ratios, in your corrected version of  
2 Illinois-American Water Company Exhibit 2.1R? What is  
3 their current financial condition as reflected on that  
4 schedule?

5 A. In 2.1R?

6 Q. Yes, the corrected version.

7 A. That I am adopting from Staff?

8 Q. Yes, uh-huh.

9 A. My recollection is it's approximately an  
10 A-, A+, A something.

11 Q. All right. On page 10 of your rebuttal  
12 testimony.

13 A. Rebuttal?

14 Q. Rebuttal, lines 18 to 21.

15 A. Yes.

16 Q. I believe there you compare pre-tax  
17 interest coverage ratio to a number representing  
18 investment grade, is that accurate?

19 A. Yes.

20 Q. Do you agree BBB is the lowest investment  
21 grade rating for pre-tax interest coverage?

22 A. I believe that's correct.

1           Q. Is this range used for a company with a  
2 business position of three?

3           A. I believe that to be true.

4           Q. Could you describe for us your use of  
5 investment grade as a limit for pre-tax interest  
6 coverage ratios?

7           A. The purpose of my testimony and the  
8 reference to pre-tax interest coverage was to  
9 demonstrate that under Staff's proposal, if there was  
10 no Savings Sharing Proposal, that the Company would be  
11 financially impaired to the point that, for example,  
12 the pre-tax interest coverage of the Company would be  
13 eroded to the point where it may be below investment  
14 grade and would barely be above the indenture  
15 requirements of the Company.

16           Q. If you could look at page 10, line 19,  
17 you have the figure 2.0 there?

18           A. Yes.

19           Q. It's my understanding that that number  
20 should be changed to 1.8, is that correct?

21           A. I believe that the range is 1.8 to 2.0,  
22 BBB.

1 MR. CLENNON: Thank you. Sorry about that.

2 EXAMINATION

3 BY EXAMINER SHOWTIS:

4 Q. Turning to your surrebuttal testimony on  
5 page 7, in your answer there you explain why the 90/10  
6 split was selected with regard to demonstrated  
7 savings. In that answer you indicate that that's what  
8 was selected to provide a return to the shareholders  
9 on and of the funds invested in the utility's assets  
10 within a reasonable time. First of all, would you  
11 tell me what you consider to be a reasonable time?

12 A. Well, the proposal was set up to insure  
13 that we were in full compliance with Section 7-204  
14 which means no adverse rate impacts to customers. And  
15 under our proposal we believe the proposal is -- the  
16 mechanics of the proposal actually guarantee savings  
17 to customers over and above the pre-acquisition level  
18 of revenue requirement. The 90 percent was chosen  
19 because that was the level that we believe was needed  
20 in order to provide the return to the Company and at  
21 the same time give meaningful savings to customers.  
22 And our schedules were put together on a 40-year

1 forward-looking basis to demonstrate the recovery of  
2 the premium and the savings back to customers.

3 Q. Did the Company have a goal, or one of  
4 the goals of its proposal was to recover a significant  
5 percentage of the acquisition adjustment within a  
6 specified period?

7 A. No. I can't say that there was a  
8 specified period that I am aware of. Again, I think  
9 the primary consideration in putting together the  
10 proposal was to insure compliance with Illinois  
11 regulations, the Public Utilities Act.

12 Q. Well, in setting up the proposal was one  
13 of the criteria, for want of a better word, that the  
14 vast majority of the savings in the early years,  
15 assuming they can be demonstrated, would be utilized  
16 to recover revenue requirements associated with the  
17 acquisition adjustment?

18 A. Well, yeah, the 90/10 sharing in the  
19 early years does certainly cause a lot of those  
20 savings to be used to cover the revenue requirement.  
21 That's still -- in my view ten percent of savings is a  
22 meaningful number.

1           Q. But the Company made a determination  
2     that, at least for the earlier years, something more  
3     than that ten percent, say 20 percent or 25 percent,  
4     would be, I guess for want of a better description,  
5     too detrimental to shareholders? In other words, they  
6     wanted to try to recover as much of the revenue  
7     requirement associated with the acquisition adjustment  
8     in the early years while providing some savings to  
9     ratepayers?

10          A. Yeah. Obviously, a different split, a  
11     lesser split, lengthens the time that it would take to  
12     recover the Company's investment.

13          Q. Just so I understand the development of  
14     the plan, was the ten percent savings for ratepayers,  
15     was that a fall out number after the Company  
16     determined what it expected or hoped to recover with  
17     regard to the acquisition revenue requirement or did  
18     it start with the decision that it wanted to flow  
19     through ten percent of the savings in the early years?  
20     I am trying to see what came first.

21          A. I am not sure my answer would directly  
22     answer your question. But, again, it's kind of a

1 combination on the one hand wanting to insure a  
2 meaningful amount of savings was provided to customers  
3 and a meaningful or a significant portion of savings  
4 was used to cover the investment that the Company had  
5 made. How specifically we got to 90/10, I can't point  
6 to an event as to how we got there.

7 Q. Did the Company, for example, run  
8 different scenarios with, say, 95/5 and the 80/20 and  
9 the 90/10, and then decided the 90/10 was the most  
10 appropriate?

11 A. I can honestly say that I don't remember  
12 other scenarios. There probably were, though.

13 EXAMINER SHOWTIS: Okay. That's all we have.

14 MR. SPRINGER: Mr. Examiner, we will have  
15 some redirect. Is it the preference we break and do  
16 that this evening or in the morning?

17 EXAMINER SHOWTIS: I think we should. Off  
18 the record.

19 (Whereupon there was then had  
20 an off-the-record discussion  
21 and the hearing was in a  
22 short recess.)

1 EXAMINER SHOWTIS: Back on the record.

2 REDIRECT EXAMINATION

3 BY MR. SPRINGER:

4 Q. Mr. Ruckman, you were asked some  
5 questions about potential test years which might be  
6 used in a future rate filing for the Citizens' areas,  
7 do you recall those questions?

8 A. Yes, I do.

9 Q. Can you tell me whether if an historical  
10 test year is used in such a filing there would be  
11 mechanisms available to reflect the effect of savings?

12 A. Yes, there would be.

13 Q. And what would that be?

14 A. Well, the Company's Savings Sharing  
15 Proposal would be implemented in the initial rate case  
16 regardless of what test year was chosen.

17 Q. And would that be through a process if an  
18 historical test year is used of pro forma adjustments?

19 A. Yes.

20 Q. There was also reference to testimony  
21 discussing a five-year interval which could elapse  
22 before the filing of rates or submission of a showing

1       regarding savings levels in the Company's rate areas.  
2       Do you have further comment with regard to your actual  
3       expectation regarding the timing of rate filings?

4               A.   We would anticipate a rate filing soon  
5       after closing.   And in that rate filing we would  
6       anticipate implementation of the Savings Sharing  
7       Proposal.

8               Q.   And do you have any comment on the areas  
9       that would be affect by that filing?

10              A.   The existing Citizens' rate areas would  
11       be impacted by that.

12              Q.   There was also a reference during  
13       questioning to the circumstances of your employment by  
14       Illinois-American Water Company subsequent to your  
15       employment by Northern Illinois Water Corporation.  
16       Would you comment on whether your position should be  
17       viewed as an additional management position?

18              A.   Yes.   Not only am I not part of the  
19       bureaucracy but in fact I am a Synergy.   There were  
20       actually, of the two separate companies, there were  
21       two vice president/treasurers or comptrollers, and now  
22       there is one.

1 Q. And that is yourself?

2 A. Correct.

3 Q. Also during questioning I believe you  
4 made reference to the revenue requirement under the  
5 Savings Sharing Proposal as being a combination of  
6 costs and savings. Would you care to clarify what you  
7 meant by that response?

8 A. Yes. It really is strictly cost-based.  
9 The revenue requirement is based on cost and the cost  
10 associated with the price paid for the assets and the  
11 savings that are used to cover those costs. And so  
12 thus it is cost-based totally.

13 Q. Finally, you were asked about the  
14 conclusion you drew from Mr. Hardas' Schedule 10.1  
15 with regard to the pre-acquisition rating which  
16 Illinois-American securities would receive. Would you  
17 further discuss your conclusion with regard to the  
18 effect of approval of the transaction without approval  
19 of the Savings Sharing Proposal on the securities  
20 rating?

21 A. Yes. There was some confusion as to  
22 whether my original answer pertained to the Company on

1 a pre-acquisition or post-acquisition basis. I wanted  
2 to make clear that on a pre-acquisition basis the  
3 financial ratios that are shown on that schedule would  
4 indicate that the Company is approximately an A+ rated  
5 company. I want to make it clear, though, that  
6 Illinois-American is not in fact rated.

7 And on a post-acquisition basis with no  
8 recovery of the Savings Sharing Proposal, the ratings  
9 in those particular financial ratios would drop in  
10 many cases to below investment grade.

11 Q. And do you have any comment on the  
12 significance that would have?

13 A. Certainly that would cause the cost of  
14 financings to be higher than they would otherwise be.  
15 It would make those financings more difficult than  
16 they would otherwise be if the Company continued in  
17 its current financial good standing.

18 MR. SPRINGER: That's all the questions we  
19 have for Mr. Ruckman at this time.

20 MR. CLENNON: If I could ask just a couple  
21 questions, Your Honor.

22

1                                    RECROSS EXAMINATION

2                                    BY MR. CLENNON:

3                                    Q.    The schedule -- the prediction that the  
4                                    Company would fall below investment grade if the  
5                                    acquisition adjustment was not allowed, does that  
6                                    prediction take into account increased revenues due to  
7                                    the increase in rates that would be anticipated after  
8                                    the rate filing?

9                                    A.    Yes, it does.

10                                  Q.    When you say, sir, that you are not a  
11                                  part of the bureaucracy or an addition to it, is it  
12                                  your testimony that a company can keep adding service  
13                                  territory without ever adding individuals to the  
14                                  corporate support system, for lack of a better phrase?

15                                  A.    Absolutely not. My testimony is that,  
16                                  however, there is no need to have duplicative  
17                                  positions for people like myself and people like HR  
18                                  directors and whole accounting departments and things  
19                                  like that.

20                                  Q.    In fact, you have determined, if I  
21                                  understand things correctly, that there is going to be  
22                                  a reduction of some employees and then the addition of

1       some employees, is that correct?

2               A.   Correct.

3               MR. CLENNON:   Very good.   That's all I have.

4               EXAMINER SHOWTIS:   You may step down.   We are  
5       going to start at 8:30 tomorrow.

6                               (Whereupon the hearing in this  
7                               matter was continued until  
8                               8:30 a.m. in Springfield,  
9                               Illinois.)

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1       STATE OF ILLINOIS       )  
  )SS  
2       COUNTY OF SANGAMON       )  
3       CASE NO.:   00-0476  
4       TITLE:   ILLINOIS-AMERICAN WATER COMPANY,  
                  CITIZENS UTILITIES COMPANY OF ILLINOIS and  
5                CITIZENS LAKE WATER COMPANY

6

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9

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10               We, Cheryl A. Davis and Carla J. Boehl, do  
11       hereby certify that we are court reporters contracted  
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15       case on the 1st day of February, 2001; that the  
16       foregoing pages are a true and correct transcript of  
17       our shorthand notes so taken as aforesaid and contain  
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19       other persons authorized by it to conduct the said  
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